

SET
A
**SELF-PACED
STUDY MATERIAL**
**CORPORATE AND
ECONOMIC LAWS**
MODULE 1 OF 2



Board of Studies (Academic)
**The Institute of Chartered
Accountants of India**

(Set up by an Act of Parliament)



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BEFORE WE BEGIN.....

The contents of the study material for Self –Paced Online Module–Set A have been designed and developed by the Board of Studies (Academic), ICAI with an objective to synchronize the syllabus with the International Education Standards (IESs) of IFAC (International Federation of Accountants) to instill and enhance the necessary pre-requisites for becoming a well-rounded, competent and globally competitive Accounting Professional.

This study material also lays emphasis on National Education Policy 2020 (NEP 2020) initiatives like conceptual clarity rather than rote learning and new pedagogical and curriculum restructuring based on the use of technology while teaching.

The liberalization and globalization of our economic policies need to be compatible with the global changes and converged to bring in various important Corporate and Economic Laws which are necessary to regulate the Corporate Sector. The dynamic nature of the economy brings in several reforms in the prevalent Corporate Laws on day to-day basis and are being amended on regular basis.

The Statutory Authorities who are in charge with the administration of these laws, clarify various issues through notification, clarifications and legislative amendments from time to time.

Requirement of Professional Knowledge and Skills

After Intermediate Level and before appearing in Final Level, you are expected to not only acquire professional knowledge but also the ability to apply such knowledge in addressing issues and solving practical problems. The integrated process of learning through academic education and practical training with help you to inculcate the requisite technical competence, professional skills and professional values, ethics and attitudes necessary for achieving the desired level of professional competence.

Significant Components of Corporate and Economic Laws

Corporate and Economic Laws is divided into two parts, namely, Part I: Corporate Laws for 70 marks and Part II: Economic Laws for 30 marks.

Part I: Corporate Laws comprise of the law and procedures under the Companies Act, 2013 and the Securities Laws covering significant provisions of the Securities Exchange Board of India Act, 1992 read *with references of SEBI (Listing Obligations and Disclosure Requirement) Regulations, 2015, SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018, SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 2011, SEBI (Prohibition of Insider Trading) Regulations, 2015.*

Part II: Economic Laws comprise of significant provisions of select economic laws namely, the Foreign Exchange Management Act, 1999, the Foreign Contribution Regulation Act, 2010, and the Insolvency and Bankruptcy Code, 2016.

In line with NEP requirements, a chapter on **e-Filing** has been included in the curriculum.

At the end of each chapter, questions have been included under the heading “Test Your Knowledge” for practice purposes.

The study material contains relevant legislative amendments of Company law, Securities Laws, and the Economic Laws made vide notifications and circulars issued upto 30th April, 2023.

Moreover, students are advised to check the Board of Studies Knowledge Portal regularly for further developments.

Framework of Chapters – Uniform Structure comprising of specific components

Efforts have been made to present the laws in a lucid manner. Care has been taken to present the chapters in a logical sequence to facilitate easy understanding by the students. The Study Material has been divided into two modules for ease of handling by students. The first module is on Corporate Laws and second module is on Securities Laws and the Economic Laws.

Each chapter of the Study Material has been structured uniformly comprising of the following components:

	Components of each Chapter	About the component
1.	Learning Outcomes	Learning outcomes which you need to demonstrate after learning each topic have been detailed in the first page of each chapter. Demonstration of these learning outcomes would help you to achieve the desired level of technical competence
2.	Content	The concepts and provisions of Corporate and Economic Laws are explained in student-friendly manner with the aid of examples/ Illustrations/diagrams /flow charts wherever possible. Diagrams and Flow charts would help you understand and retain the concept/provision learnt in a better manner. Examples would help you understand the application of concepts/provisions. These value additions would, thus, help you develop conceptual clarity and get a good grasp of the topic.

3.	Test Your Knowledge	The exercise questions and answers would help you to analyse the provisions of Corporate and Economic Laws and apply the same in problem solving, thus, sharpening your application skills. In effect, these questions would test your ability to analyse, interpret and apply the concepts/provisions learnt in solving problems and addressing issues. Multiple choice questions and small case scenarios in the theoretical/descriptive questions have also been given to test your conceptual understanding/ analytical ability and interpretational skills.

We hope that these student-friendly features in the Study Material makes your learning process more enjoyable, enriches your knowledge and sharpens your application and Interpretational skills.

Happy Reading and Best Wishes!

SYLLABUS- SELF PACED

SET A

PAPER: CORPORATE AND ECONOMIC LAWS (100 MARKS)

PART-I: CORPORATE LAWS (70 Marks)

SECTION A: COMPANY LAW (50 Marks)

Objective:

To acquire the ability to analyse, interpret and apply the provisions of the Company Law in practical situations.

Contents:

The Companies Act, 2013 and Rules framed thereunder in its entirety with specific reference to section 149 onwards:

- (i) Appointment and Qualifications of Directors
- (ii) Appointment and Remuneration of Managerial Personnel
- (iii) Meetings of Board and its Powers
- (iv) Inspection, Inquiry and Investigation
- (v) Compromises, Arrangements and Amalgamations
- (vi) Prevention of Oppression and Mismanagement
- (vii) Winding Up
- (viii) Miscellaneous Provisions
- (ix) Adjudication, Special Courts, National Company Law Tribunal
- (x) e-Filing

SECTION B: SECURITIES LAWS (20 Marks)

Objective:

To acquire the ability to analyse the significant provisions of the **SEBI Act**.

Contents:

Overview of the Securities Exchange Board of India Act, 1992, and references of following Regulations:

- (i) SEBI (Listing Obligations and Disclosure Requirement) Regulations, 2015
- (ii) SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018
- (iii) SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 2011
- (iv) SEBI (Prohibition of Insider Trading) Regulations, 2015

PART II: ECONOMIC LAWS (30 MARKS)

Objective:

To acquire the ability to analyse the significant provisions of select Economic Laws.

Contents:

1. **The Foreign Exchange Management Act, 1999 and significant Rules and Regulations:** Introduction, Broad structure of FEMA, Definition, Regulation and Management of Foreign Exchange, Contraventions and Penalties in brief, Miscellaneous Provisions.
2. **The Foreign Contribution Regulation Act, 2010 and its Regulation:** Definitions, Regulation of Foreign Contribution and Miscellaneous Provisions.
3. **The Insolvency and Bankruptcy Code, 2016 and significant Rules and Regulations:** Significant concepts covered uptill section 33 of the Code.

Note: *If new legislations are enacted in place of the existing legislations, the syllabus would include the corresponding provisions of such new legislations with effect from a date notified by the Institute.*

The specific inclusions / exclusions in the various topics covered in the syllabus will be affected every year by way of study guidelines, if any.

CONTENTS

PART I: CORPORATE LAWS

SECTION A: COMPANY LAW

MODULE – 1

- Chapter 1: Appointment and Qualifications of Directors
- Chapter 2: Appointment and remuneration of Managerial Personnel
- Chapter 3: Meetings of Board and its powers
- Chapter 4: Inspection, inquiry and Investigation
- Chapter 5: Compromises, Arrangements and Amalgamations
- Chapter 6: Prevention of Oppression and Mismanagement
- Chapter 7: Winding Up
- Chapter 8: Miscellaneous Provisions
- Chapter 9: Compounding of offences, Adjudication, Special Courts, National Company Law Tribunal and Appellate Tribunal
- Chapter 10: e-Filing

SECTION B: SECURITIES LAWS

MODULE – 2

- Chapter 1: The Securities Exchange Board of India Act, 1992 and SEBI (Listing Obligations and Disclosure Requirement) Regulations, 2015, SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018, SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 2011, SEBI (Prohibition of Insider Trading) Regulations, 2015.

PART II: ECONOMIC LAWS

- Chapter 1: The Foreign Exchange Management Act, 1999
- Chapter 2: The Foreign Contribution Regulation Act, 2010
- Chapter 3: The Insolvency and Bankruptcy Code, 2016

DETAILED CONTENTS: MODULE-1

PART I: CORPORATE LAWS

SECTION A: COMPANY LAW

Page No.

CHAPTER-1: APPOINTMENT AND QUALIFICATION OF DIRECTORS

1.	Introduction	1.2
2.	Company to have Board of Directors	1.3
3.	Appointment of Directors.....	1.6
4.	Director Identification Number (DIN).....	1.12
5.	Right of persons other than retiring directors to stand for directorship.....	1.19
6.	Appointment of Directors elected by Small shareholders.....	1.21
7.	Appointment of additional director, alternate director, a director to fill casual vacancy and nominee director.....	1.23
8.	Appointment of directors to be voted individually	1.28
9.	Option to adopt principle of proportional representation for appointment of directors.....	1.30
10.	Disqualifications for appointment of director	1.31
11.	Maximum number of directorship.....	1.33
12.	Independent Directors.....	1.35
13.	Manner of selection of independent directors and maintenance of data bank of independent directors	1.43
14.	Duties of Directors	1.47
15.	Vacation of office of director	1.49
16.	Resignation of Director	1.50
17.	Removal of Directors	1.51

18.	Register of Directors and Key Managerial Personnel and their shareholding	1.54
19.	Members' right to inspect	1.56
20.	Punishment.....	1.57
	Test Your Knowledge	1.58

CHAPTER-2: APPOINTMENT AND REMUNERATION OF MANAGERIAL PERSONNEL

1.	Introduction	2.2
2.	Appointment of Managing Director, Whole Time Director or Manager	2.4
3.	Appointment of Key Managerial Personnel	2.9
4.	Functions of Company Secretary.....	2.13
5.	Company to Fix Limit with Regard to Remuneration.....	2.14
6.	Overall maximum managerial remuneration and managerial remuneration in case of absence or inadequacy of profits.....	2.15
7.	Recovery of managerial remuneration in certain cases	2.29
8.	Calculation of profits	2.29
9.	Forms of, and procedure in relation to, certain applications	2.31
10.	Compensation for loss of office of managing or whole-time director or manager	2.32
11.	Secretarial Audit for bigger companies	2.34
12.	Part II, Part III and Part IV of Schedule V	2.36
	Test Your Knowledge	2.40

CHAPTER-3: MEETINGS OF BOARD AND ITS POWERS

1.	Introduction	3.2
2.	Meetings of Board.....	3.2
3.	Quorum for meetings of Board	3.12
4.	Passing of resolution by circulation	3.15
5.	Audit Committee, Vigil Mechanism and Punishment.....	3.17
6.	Nomination and Remuneration Committee and Stakeholders Relationship Committee and punishment	3.23

7.	Powers of Board	3.27
8.	Restrictions on powers of Board.....	3.31
9.	Company to contribute to bona fide and charitable funds, etc.	3.35
10.	Prohibitions and restrictions regarding political contributions	3.36
11.	Power of Board and other persons to make contributions to National Defence Fund, etc.	3.39
12.	Disclosure of interest by director.....	3.39
13.	Defects in appointment of directors not to invalidate actions taken.....	3.42
14.	Loan to directors, etc.	3.44
15.	Loan and Investment by Company.....	3.47
16.	Investments of company to be held in its own name	3.53
17.	Related Party Transactions	3.55
18.	Register of contracts or arrangements in which directors are interested	3.64
19.	Contract of employment with managing or whole- time directors	3.66
20.	Payment to director for loss of office, etc., in connection with transfer of undertaking, property or shares.....	3.67
21.	Restriction on non-cash transactions involving directors	3.69
22.	Contracts by One Person Company.....	3.71
	Test Your Knowledge	3.72

CHAPTER-4: INSPECTION, INQUIRY AND INVESTIGATION

1.	Introduction	4.2
2.	Power to call for information, inspect books and conduct inquiries	4.3
3.	Conduct of inspection and inquiry.....	4.7
4.	Report on inspection made.....	4.8
5.	Search and seizure	4.9
6.	Investigation into affairs of company	4.11
7.	Establishment of Serious Fraud Investigation Office	4.13
8.	Investigation into affairs of Company by Serious Fraud Investigation Office	4.14
9.	Investigation into company's affairs in other cases	4.19

10.	Security for payment of costs and expenses of investigation.....	4.20
11.	Firm, body corporate or association not to be appointed as inspector	4.21
12.	Investigation of ownership of company	4.21
13.	Procedure, powers, etc., of inspectors.....	4.22
14.	Protection of employees during investigation	4.25
15.	Power of inspector	4.27
16.	Powers of tribunal	4.29
17.	Inspector's report.....	4.31
18.	Actions to be taken in pursuance of inspector's report	4.31
19.	Expenses of investigation	4.33
20.	Voluntary Winding up of Company, etc., not to stop Investigation Proceedings	4.34
21.	Legal Advisers and bankers not to disclose certain information.....	4.34
22.	Investigation etc. of foreign companies.....	4.35
23.	Penalty for furnishing false statement, mutilation, destruction of documents	4.35
	Test Your Knowledge	4.36

CHAPTER-5: COMPROMISES, ARRANGEMENTS AND AMALGAMATIONS

1.	Introduction	5.2
2.	Power to Compromise or Make Arrangements with Creditors and Members	5.6
3.	Power of Tribunal to enforce compromise or arrangement	5.13
4.	Merger and Amalgamation of Companies	5.15
5.	Power to Acquire Shares of Shareholders Dissenting from Scheme or Contract Approved by Majority	5.20
6.	Purchase of Minority Shareholding	5.23
7.	Power of Central Government to Provide for Amalgamation of Companies in Public Interest	5.26
8.	Registration of offer of Schemes involving transfer of shares	5.29
9.	Preservation of Books and Papers of Amalgamated Companies	5.30

10.	Liability of Officers in Respect of Offences Committed Prior to Merger, Amalgamation, etc.	5.30
11.	Fast track mode of merger or amalgamation of certain companies	5.30
12.	Merger or Amalgamation of Company with foreign company	5.35
	Test Your Knowledge	5.37

CHAPTER-6: PREVENTION OF OPPRESSION AND MISMANAGEMENT

1.	Introduction	6.2
2.	Application to Tribunal for Relief in Cases of Oppression, etc.	6.5
3.	Right to apply under section 241	6.9
4.	Powers of Tribunal	6.11
5.	Consequences of termination or modification of certain agreements	6.14
6.	Class action	6.15
7.	Application of certain provisions to proceedings under section 241 or section 245	6.19
	Test Your Knowledge	6.20

CHAPTER-7: WINDING UP

1.	Introduction	7.2
2.	Modes of Winding Up	7.2
3.	Circumstances in Which Company May be Wound Up by Tribunal	7.2
4.	Petition for Winding up	7.4
5.	Powers of Tribunal	7.6
6.	Directions for Filing Statement of Affairs	7.7
7.	Company Liquidators and their appointments	7.8
8.	Removal and Replacement of Liquidator	7.9
9.	Intimation to Company Liquidator, Provisional Liquidator and Registrar	7.10
10.	Effect of Winding up order	7.13
11.	Stay of Suits, etc., on Winding up Order	7.13
12.	Jurisdiction of Tribunal	7.14

13.	Submission of Report by Company Liquidator	7.14
14.	Directions of Tribunal on Report of Company Liquidator	7.15
15.	Custody of Company's Properties	7.16
16.	Promoters, Directors, etc., to cooperate with Company Liquidator	7.17
17.	Settlement of List of Contributories and Application of Assets	7.18
18.	Obligations of Directors and Managers	7.19
19.	Advisory Committee	7.19
20.	Submission of Periodical Reports to Tribunal	7.20
21.	Powers and Duties of Company Liquidator	7.21
22.	Provision for Professional Assistance to Company Liquidator	7.24
23.	Exercise and Control of Company Liquidator's Powers	7.24
24.	Books to be kept by Company Liquidator	7.25
25.	Audit of Company Liquidator's Accounts	7.26
26.	Payment of Debts by Contributory and Extent of Set-off	7.27
27.	Power of Tribunal to Make Calls	7.27
28.	Adjustment of Rights of Contributories	7.28
29.	Power to Order Costs	7.28
30.	Power to Summon Persons Suspected of Having Property of Company, etc.....	7.28
31.	Power to Order Examination of Promoters, Directors, etc.	7.29
32.	Arrest of Person Trying to Leave India or Abscond	7.31
33.	Dissolution of Company by Tribunal	7.32
34.	Appeals from Orders Made Before Commencement of Act	7.33
35.	Debts of all Descriptions to be Admitted to Proof	7.33
36.	Overriding Preferential Payments	7.34
37.	Preferential Payments	7.36
38.	Fraudulent Preference	7.38
39.	Transfers Not in Good Faith to be Void	7.39
40.	Certain Transfers to be Void	7.40

41.	Liabilities and Rights of Certain Persons Fraudulently Preferred	7.40
42.	Effect of Floating Charge	7.41
43.	Disclaimer of Onerous Property	7.41
44.	Transfers, etc., after Commencement of Winding Up to be Void	7.44
45.	Certain Attachments, Executions, etc., in Winding Up by Tribunal to be Void	7.44
46.	Offences by Officers of Companies in Liquidation	7.45
47.	Statement that Company is in Liquidation	7.47
48.	Books and Papers of Company to be Evidence	7.48
49.	Inspection of Books and Papers by Creditors and Contributories	7.48
50.	Disposal of Books and Papers of Company	7.48
51.	Company Liquidation Dividend and Undistributed Assets Account	7.49
52.	Liquidator to Make Returns, etc.	7.52
53.	Meetings to Ascertain Wishes of Creditors or Contributories	7.52
54.	Court, Tribunal or Person, etc., Before Whom Affidavit May be Sworn	7.53
55.	Powers of Tribunal to Declare Dissolution of Company Void	7.53
56.	Commencement of Winding Up by Tribunal	7.54
57.	Exclusion of Certain Time in Computing Period of Limitation	7.54
	Test Your Knowledge	7.55

CHAPTER 8: MISCELLANEOUS PROVISIONS

1.	Introduction	8.2
2.	Registered Valuer	8.2
3.	Removal of Names of Companies from the Register of Companies	8.13
4.	Government Companies	8.19
5.	Nidhis	8.21
6.	Miscellaneous Provisions	8.31
	Test Your Knowledge	8.36

CHAPTER 9: ADJUDICATION, SPECIAL COURTS, NATIONAL COMPANY LAW TRIBUNAL & NATIONAL COMPANY LAW APPELLATE TRIBUNAL

1.	Introduction	9.2
2.	NCLT and NCLAT	9.3
3.	Special Court	9.12
4.	Offences to be non-cognizable	9.15
5.	Compounding of certain offences.....	9.16
6.	Mediation and Conciliation Panel.....	9.19
7.	Serious Fraud Investigation Office	9.20
8.	Power of Central Government to Appoint Company Prosecutors	9.21
9.	Appeal against Acquittal	9.21
10.	Compensation for Accusation without Reasonable Cause	9.21
11.	Application of fines	9.21
12.	Factors for determining level of punishment.....	9.21
13.	Lesser penalties for One Person Companies or small companies	9.22
14.	Adjudication of penalties	9.22
15.	Penalty for repeated default.....	9.26
	Test Your Knowledge	9.27

CHAPTER 10 : e-FILING

1.	Introduction	10.2
2.	Provisions Relating to Filing of Applications, Documents, Inspection, etc., in Electronic Form	10.4
3.	Electronic form to be exclusive, alternative or in addition to physical form.....	10.30
4.	Provision of Value-Added Services Through Electronic Form	10.31
5.	Application of Provisions of Information Technology Act, 2000	10.31
6.	Fee for Filing etc.	10.31
7.	MCA21 Version 3.0	10.44
8.	Case Studies relating to Ethics.....	10.45
	Test Your Knowledge	10.58

CHAPTER

1

APPOINTMENT AND QUALIFICATIONS OF DIRECTORS



LEARNING OUTCOMES

By the end of this chapter, students will be able to:

- ❑ Comprehend the provisions relating to the appointment of directors, number of directors, resident director, appointment of woman director and others.
- ❑ Explain the Director Identification Number (DIN), its allotment and other matters relating to DIN.
- ❑ Elaborate as to who are Independent Directors, their appointment, qualifications, tenure etc.
- ❑ Specify and recognise the provisions relating to the first director, additional director, alternate director, nominee director and casual vacancy of the director.
- ❑ Explain the provisions relating to small shareholders' director, retirement by rotation, principle of proportional representation for appointment, maximum directorships etc.
- ❑ Describe the disqualifications pertaining to the appointment as director, duties of directors, vacation of office of director, resignation of director, removal of director, etc.



1. INTRODUCTION

According to Section 2(10) of the Companies Act, 2013 (in short 'the Act'), "**Board of Directors**" or "**Board**", in relation to a company, means the collective body of the directors of the company.

According to section 2(34) "**director**" means a director appointed to the Board of a company.

The directors are the individuals who are appointed to manage the business affairs of a company. A company is an artificial person created by law having separate legal existence but without any physical body or mind of its own. It needs to be managed through the human beings. Though the shareholders being owners are physically available to manage their company but as their number grows, all of them together may not be able to manage the affairs; and if they do so it shall be mismanagement and nothing else. That's why the concept of directors has emerged. The directors (within the permissible limit) may be elected from among the shareholders or outsiders.

Legal position of Directors

As regards legal position of directors in relation to a company, they can be considered both agents and trustees. As agents, they bind the company as their principal as soon as they enter into various transactions on its behalf. The law of agency comes into play and it governs the relationship between the company and its directors. At times, the company itself is principal as well as agent in respect of certain acts which cannot be delegated. The Companies Act, 2013 lays down provisions requiring as to when the company needs to act both as principal as well as agent and when the directors need to act as agent of the company. It may be noted that where directors are empowered to take certain decisions, the company cannot negate them or issue directions to the directors directing them to go for a particular decision except that it may replace the directors with the ones of its choice. As trustees, the directors are required to take care of properties, moneys, trade secrets, etc. belonging to the company. In fact, as trustees the directors are in a fiduciary relationship with the company (and not with any individual shareholder) and if such relationship is broken and the company suffers losses because of the illegal acts of the directors, the erring directors will be required to compensate the losses suffered by the company. The office of directorship is an office of trust.

The definition of '**officer**' given in Section 2 (59) of the Act, *inter-alia*, includes '**director**' which means a director, at certain times, is also the officer of the company. Since an officer is an employee of the company, the director as officer is also an employee so far as certain provisions of the Companies Act, 2013 are concerned.

Collective body of the directors

The collective body of the directors is called the '**Board of Directors**' or simply the '**Board**'.

It is the Board which takes decisions at its meetings and not any individual director. This is the reason why a quorum (*i.e.* presence of minimum directors at the Board meetings) is prescribed so that collective decisions are taken. At times, if permitted, the decisions can be taken by the Board without calling a meeting but in that case too they are collective decisions.



2. COMPANY TO HAVE BOARD OF DIRECTORS[SECTION 149]

Section 149 of the Act contains provisions which require that every company shall have to constitute Board of Directors. The provisions of constitution of Board of Directors are stated as under:

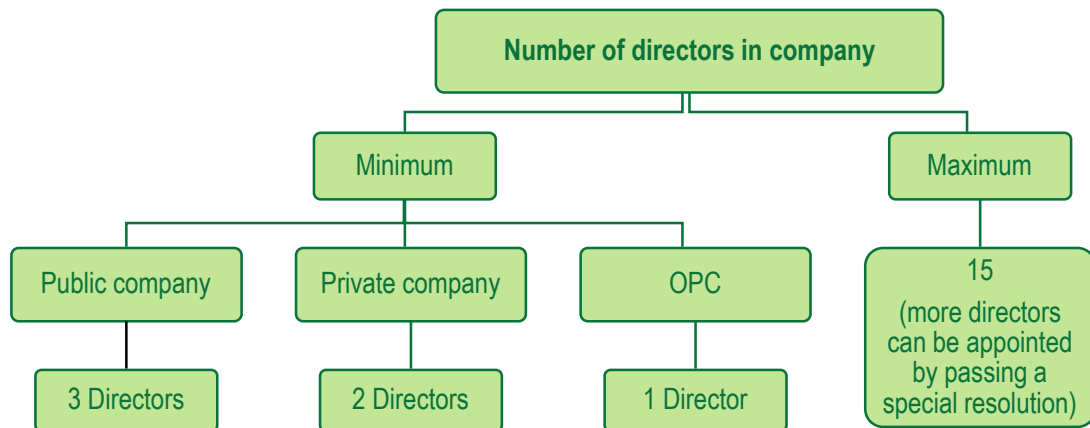
Number of Directors: According to section 149(1) of the Companies Act, 2013, every company shall have a Board of Directors consisting of **individuals as directors**. Thus, any person other than individuals like a body corporate, firm or association of persons cannot be appointed as a director.

Every company shall have-

- (a) **minimum number of directors:**
- (A) in case of a Public Company-3 Directors,
 - (B) in case of a Private Company-2 Directors, and
 - (C) in case of a One Person Company (OPC)-1 Director
- (b) **maximum number of directors:** 15 Directors



Note: If the company wants to appoint more than 15 directors, it can do so after passing a special resolution.



Exemptions

- (A) A **Government company** is exempted:
- (i) from the application of Section 149 (1) (b) which requires a company to have a maximum of fifteen directors only; and
 - (ii) from the application of First Proviso to Section 149 (1) which enables a company to appoint more than fifteen directors after passing a special resolution.

However, above exemption is applicable only if such Government company has not committed a default in filing its financial statements under Section 137 or Annual return under

Section 92 with the registrar. [Notification No. G.S.R. 463(E), dated 5th June, 2015 as amended by Notification No. GSR 582 (E), dated 13-06-2017].

(B) Similar exemption, as above, is also applicable to company incorporated under **Section 8 of the Companies Act, 2013** subject to the condition that such a company has not committed a default in filing its financial statements under Section 137 or Annual return under Section 92 with the registrar. [Notification No. 466 (E), dated 5th June, 2015 (as amended by Notification No. 584 (E), dated 13th June, 2017)].

- (c) **Woman director:** At least one woman director shall be on the Board of such class or classes of companies as has been prescribed in Rule 3 of the Companies (Appointment and Qualifications of Directors) Rules, 2014 [**Second proviso to section 149(1)**]

Rule 3 provides that the following classes of companies shall appoint at least one woman director-



every listed company

every other public company having

- paid up share capital of 100 crore or more, or
- turnover of 300 crore or more

*Explanation-*For the purposes of having a woman director on the board, it is clarified that the paid up share capital or turnover, as the case may be, as on the last date of latest audited financial statements shall be taken into account.

Compliance by a newly incorporated company: A company, which has been incorporated under the Act and is covered by the provisions requiring appointment of a woman director, shall comply with such provisions within a period of six months from the date of its incorporation.

Filling of Intermittent Vacancy of Woman Director: Any intermittent vacancy of a woman director shall be filled-up by the Board at the earliest but not later than **immediate next Board Meeting or 3 months** from the date of such vacancy whichever is later.

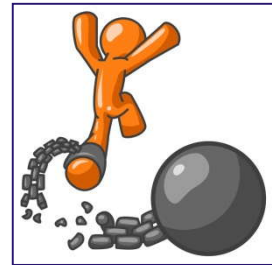
Example 1: Sheetal was occupying the office of woman director in a company but due to her sudden death on 17th March, 2019, the intermittent vacancy so occurred was required to be filled-up at the earliest because she was the only woman director on the board. The immediate Board meeting was held on 25th June, 2019. The vacancy of the women director must be

filled-up latest by 25th June, 2019 or within three months from the date of such vacancy i.e. 16th June, 2019 whichever is later i.e., by 25th June 2019.

- (d) **Resident Director:** Every company shall have at least one director who stays in India for a total period of not less than one hundred and eighty-two days during the financial year.

However, in case of a newly incorporated company the above requirement shall apply proportionately at the end of the financial year in which it is incorporated. [Section 149(3)]

- (e) **Independent Director:** Specified public companies are required to appoint independent directors on their Board with a view to boost the level of corporate governance. Such Specified companies are the backbone of any economy and therefore, they must be managed in the best possible manner including adhering to the specified legal provisions. An independent director needs to have an independent mindset which should not be unduly influenced by the other members of the Board; and if such members take any decision which is illegal or not in the best interest of the company or economy, it must be hindered by the independent directors at the outset. The provisions relating to independent directors are discussed later in the Chapter.



- (f) **Interested Director:** An interested director is one among the other directors who constitute Board of Directors. In fact, when an existing director becomes interested in a transaction of the company, he is called interested director; and he needs to disclose his interest at the appropriate forum and at appropriate time. The provisions regarding interested director are discussed in another Chapter.

- (g) **Executive and Non-Executive Directors:** The Board of Directors may comprise both executive and non-executive directors. The executive directors are responsible for managing different business operations undertaken by the company. It is their responsibility that the departments which they head operate smoothly. A whole time director and managing director are covered in this category of directors. In contrast, the non-executive directors participate through Board meetings in discussions relating to framing of policies for the efficient management of the company. Professional directors and nominee directors are covered in this category of directors. Independent directors are a type of non-executive directors. They are not as active as executive directors on the board of the company. They are held to be liable only if they knowingly consented to the wrongful acts.



3. APPOINTMENT OF DIRECTORS [SECTION 152]

Section 152 of the Act deals with the matters relating to appointment of directors.

(i) Appointment of First Directors

Where no provision is made in the articles of a company for the appointment of the first directors, the **subscribers to the memorandum** who are individuals shall be deemed to be the first directors of the company until the directors are duly appointed. [Section 152(1)]

In case of a One Person Company (OPC), **an individual being member** shall be deemed to be its first director until the director or directors are duly appointed by the member in accordance with the provisions of this section.[Section 152(1)]

In simple words, usually, articles of the company contain the names of the first directors. In case it is not so, then the individual subscribers to the memorandum are deemed to be the first directors. The corporate bodies, if they are also subscribers, shall not be capable of becoming directors. The first directors shall hold the office until the directors are duly appointed. In fact, the term of first directors is limited to the holding of first Annual General Meeting (AGM). So far as OPC is concerned, the individual member of the OPC is deemed as first director. Thereafter, such member may appoint director or directors as per his requirements.



(ii) Appointment of subsequent Directors

Save as otherwise expressly provided in this Act, every director shall be appointed by the company in general meeting. [refer Section 152(2)]

At a general meeting, the shareholders of the company (*i.e.* the owners) gather and take decisions. Generally, every director shall be appointed by the company in general meeting except where the Companies Act expressly provides some other procedure for appointment of directors.

For **example**, it is expressly provided in the Act that additional directors or alternate directors can be appointed by the Board of Directors if the articles of the company empower Board in this respect¹.

(iii) Other Requirements of Appointment

(a) **Allotment of Director Identification Number (DIN):** A person shall be appointed as a director of a company only when he has been allotted DIN under section 154 or any other number as may be prescribed under section 153. [refer Section 152(3)]

¹ As per Section 161, explained later on.

APPOINTMENT AND QUALIFICATIONS OF DIRECTORS

1.7

- (b) **Providing of DIN and furnishing of Declaration by the proposed Director:** Every person proposed to be appointed as a director by the company in general meeting or otherwise, shall furnish his Director Identification Number (DIN) or such other number as may be prescribed under Section 153. Further, he shall also furnish a declaration that he is not disqualified to become a director under this Act. [refer Section 152(4)]
- (c) **Written Consent to act as Director:** A person appointed as a director shall not act as a director unless he gives his written consent to hold the office as a director. The consent shall be furnished to the company on or before his appointment as a director in Form DIR-2.

The company shall file the consent of the director with the Registrar within 30 days of such appointment in Form DIR-12 along with the prescribed fee as prescribed [refer Section 152 (5) and Rule 8 of the Companies (Appointment and Qualifications of Directors) Rules, 2014].

Provided further that in case the person seeking appointment is a national of a country which shares land border with India, necessary security clearance from the Ministry of Home Affairs, Government of India shall also be attached along with the consent.

Example 2: Mr. Naresh wants to appoint himself as director in Global Services Private Limited. Mr. Naresh is required to apply for DIN (if he does not have the DIN) thereafter, he can be appointed as a director in Global Services Private Limited by giving written consent in Form DIR-2 to the company.

Global Services Private Limited shall have to file the consent of Mr. Naresh with the Registrar within 30 days of such appointment in Form DIR-12.

- (d) **Explanatory Statement in case of appointment of Independent Director:** In case an independent director is appointed in the general meeting, an explanatory statement for such appointment annexed to the notice for the general meeting, shall include a statement that in the opinion of the Board, he fulfills the conditions specified in this Act for such an appointment [refer Proviso to Section 152 (5)].

Exemptions

Non-applicability of Section 152 (5):

(1) Section 152 (5) regarding 'furnishing of consent to act as a director' shall not apply in case of **Government company** where appointment of the director is done by the Central Government or State Government. [Notification No. G.S.R. 463(E), dated 5th June, 2015 as amended by Notification No. GSR 582 (E), dated 13-06-2017].

(2) Similar exemption from Section 152(5) is also applicable to a **section 8 company**. [Notification No. 466 (E), dated 5th June, 2015 as amended by Notification No. 584 (E), dated 13th June, 2017].

Note: In both the above cases, the exemption is applicable only if the company has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar.

(iv) **Retirement of Directors by Rotation [Section 152(6)]**

Section 152 (6) deals with retirement of directors by rotation. The reason behind incorporation of such a provision in the Statute is that at no stage a self-perpetuating management should take control of the company. Under the model of self-perpetuating management, the Board of Directors is allowed to control its own composition i.e. such board can dictate the terms like how long a director can serve, and even it can elect and re-elect directors itself. This type of model may not be conducive to the healthy growth of the company. In effect, shareholders are the owners of the company but they cannot usurp the powers of the directors and interfere in the matters of managing the company. The concept of rotational directors enables them not to re-elect a retiring director for whom they have an unfavourable opinion.

The provisions of Section 152 (6) are stated as under:

- (a) **Appointment of Rotational director & no. of directors liable to retire by rotation:** Unless the articles provide for the retirement of all directors at every annual general meeting, not less than two-thirds of the total number of directors of public company shall—
 - (A) be persons whose period of office is liable to determination by retirement of directors by rotation; and
 - (B) save as otherwise expressly provided in this Act, be appointed by the company in general meeting.
- (b) **Appointment of non-rotational directors:** The remaining directors in the case of any such company shall, in default of, and subject to any regulations in the articles of the company, also be appointed by the company in general meeting.
- (c) **Retirement from office of rotational director:** At the first annual general meeting of a public company held next after the date of the general meeting at which the first directors are appointed and at every subsequent annual general meeting, one-third of such of the directors for the time being as are liable to retire by rotation, or if their number is neither three nor a multiple of three, then, the number nearest to one-third, shall retire from office.

It is to be noted that the provision regarding 'retirement by rotation' is applicable to a public company or a private company which is subsidiary of a public company. In other words, a private limited company which is not a subsidiary of a public company, is exempted and therefore, if the articles permit it can appoint all its directors as non-rotational directors or permanent directors.

The articles of a public company may provide for the retirement of all the directors at every annual general meeting. If such is not the case, then not less than two-thirds of the total number of directors of that public company shall be the persons who are liable to retire by rotation. In other words, the articles must provide that minimum two-thirds of the total number of directors shall be liable to retirement by rotation. Such directors are called rotational directors.

The term “**total number of directors**” shall not include independent directors, whether appointed under the Companies Act, 2013 or any other law for the time being in force, on the Board of a company. Thus, independent directors are not liable to retire by rotation and therefore, they are non-rotational directors.

²Further, any person appointed as a nominee director being nominated by any institution in pursuance of the provisions of any law or any agreement (like when a financial institution that has been created by an Act of Parliament nominates a person as its nominee director on the Board of a company which has availed financial assistance from such institution) cannot be considered as a director liable to retire by rotation. Nominee director may also be appointed by the Central Government or the State Government by virtue of its shareholding in a Government company.

One-third of directors to retire at AGM: Once the number of directors who are liable to retire by rotation is determined, only one-third out of that number shall retire. If such number is neither three nor a multiple of three, then, the number nearest to one-third, shall be considered and such of the directors shall retire from office.

Example 3: Khatkhata Advisory Limited constituted its board with 12 directors in which 2 directors are independent directors and 1 director is a nominee director. As per the provision of section 152 of the Companies Act, 2013, the concept of retirement by rotation of rotational directors shall be applicable to public company. Therefore, Khatkhata Advisory Limited shall be required to calculate the number of rotational directors which is liable to retire by rotation.

Total number of directors who are holding their office is 12 directors. It should be noted that at least $\frac{2}{3}$ rd of total number of directors shall be liable to retire by rotation. However, independent director and nominee director shall not be counted in “total number of the directors”. Thus, 12 Directors less 3 Directors i.e. 9 directors shall be counted for “total number of the directors”.

Here, 6 directors ($9 \times \frac{2}{3}$ rd = 6) shall be liable to retire by rotation. Now, $\frac{1}{3}$ rd of directors liable to retire by rotation (i.e. $6 \times \frac{1}{3}$ rd = 2 directors), shall actually retire by rotation at AGM.

² Refer Section 161 (3).

Example 4: A company is having 6 directors.

Directors liable to retire by rotation: $6 \times \frac{2}{3}$ i.e. 4

No. of directors to retire at AGM: $4 \times \frac{1}{3}$, i.e. 1.33 or nearest to $\frac{1}{3}$ rd is 1.

Example 5: A company is having 7 directors.

Directors liable to retire by rotation $7 \times \frac{2}{3}$ i.e. 4.7 or 5 (not less than two-third)

No. of directors to retire at AGM: $5 \times \frac{1}{3}$ i.e. 1.67 or nearest to $\frac{1}{3}$ rd is 2.

Example 6: A company is having 9 directors out of which 3 are independent directors. The 'total number of directors' for the purpose of calculation of number of rotational directors shall be 6 only because 3 independent directors are to be excluded. Rest of the calculations shall be as per Example given above.

- (d) **Directors liable to retire by rotation:** The directors who actually retire by rotation at every annual general meeting shall be those who have been longest in office since their last appointment. If two or more directors were appointed on the same day, retirement by rotation will be decided between them by mutual agreement among themselves or by lot as the case may be.

The above provision (d) clarifies the basic question that after the determination of number of directors liable to retire by rotation, who should actually retire at the AGM? For this purpose it is provided that the directors who have been longest in the office since their last appointment are the directors who need to be retired first. However, it may happen that some of those were appointed as directors on the same day. In that case, if there exists any mutual understanding relating to retirement among such directors, that should be followed; otherwise the determination shall be done by draw of lots.

- (e) **Filling of vacancy of rotational director:** At the annual general meeting at which a director retires as aforesaid, the company may fill up the vacancy by appointing the retiring director or some other person thereto.

Re-appointment: When a director is retired a vacancy is created. To fill that vacancy, the company may re-appoint the retiring director itself at the AGM. If the retiring director is not re-appointed, the company may appoint some other person at his place but in that case provisions of Section 160³ are to be complied with.

The clause regarding appointment of directors for filling the vacancies created by retiring directors is quite important. However, the number of directors should not fall short of minimum directors required in a company at any stage. However, so long as

³ Section 160 is discussed later in the Chapter.

the clause regarding minimum required directors is fulfilled the company may also resolve not to appoint anyone in place of retiring director.

In case Annual General Meeting is not held on due date, then the retirement of rotational directors cannot be postponed to that particular date when the AGM shall be held in future. The directors who are liable to retire must vacate the office of director immediately when the AGM is ought to have been held.

Non-rotational Directors: Remaining $1/3^{\text{rd}}$ or less number of total directors (after determining the number of rotational directors) are not liable to retire by rotation. These are called non-rotational directors. They may also be appointed at the general meeting or as per the provisions contained in the articles of the company.

(v) **Deemed re-appointment of retiring Directors under certain circumstances [Section 152(7)]**

Section 152 (7) provides the way for deemed appointment of a retiring director as under:

- (a) **Adjournment of general meeting:** If the vacancy of the retiring director is not so filled-up and the meeting has not expressly resolved not to fill the vacancy, the meeting shall stand adjourned till the same day in the next week, at the same time and place.

In case that day is a national holiday, the meeting shall be adjourned till the next succeeding day which is not a holiday, at the same time and place.

- (b) **Deemed re-appointment:** If at the adjourned meeting also, the vacancy of the retiring director is not filled up and that meeting also has not expressly resolved not to fill the vacancy, the retiring director shall be deemed to have been re-appointed at the adjourned meeting with immediate effect.

Exceptions to deemed re-appointment: In the following circumstances, a retiring director shall not be deemed as re-appointed:

- (A) if at that meeting or at the previous meeting, a resolution for the re-appointment of such director has been put to the meeting and lost *i.e.* his re-appointment has not been considered favourably because of non-passing of resolution;
- (B) if the retiring director has, by a notice in writing addressed to the company or its Board of directors, expressed his unwillingness to be so re-appointed;
- (C) if he is disqualified for appointment as per the provisions of the Act;
- (D) if a resolution, whether special or ordinary, is required for his appointment or re-appointment by virtue of any provisions of this Act; or
- (E) if Section 162 is applicable to the case *i.e.* where a single resolution was used to appoint two or more persons as directors without first moving a proposal which was required to be agreed to at the meeting and no vote was being cast

against it. In such a case, Section 162 is contravened and two or more appointments made by a single resolution are void. Consequently, retiring director is not deemed to be re-appointed.

Note: For the purposes of Section 152, the “retiring director” means a director retiring by rotation⁴.

Exemptions

Non-applicability of Sections 152(6) and 152(7): Section 152(6) and 152 (7) of the Act of 2013, shall not apply to:

- (a) a Government company, which is not a listed company, in which not less than fifty-one per cent of paid up share capital is held by the Central Government, or by any State Government or Governments or by the Central Government and one or more State Governments;
- (b) a subsidiary of a Government company, referred to in (a) above.

subject to the condition that such a company has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar.

[Notification No.G.S.R. 463(E), dated 5th June, 2015 as amended by Notification No. GSR 582 (E), dated 13-06-2017].



4. DIRECTOR IDENTIFICATION NUMBER (DIN) [SECTION 152 (3) AND SECTIONS 153 TO 159]

“Director Identification Number” (DIN)⁵: DIN means an identification number allotted by the Central Government to any individual, intending to be appointed as director or to any existing director of a company, for the purpose of his identification as a director of a company.

It is provided that the Director Identification Number (DIN) obtained by the individuals prior to the notification of the ‘Specification of Definitions Details Rules’ shall be the DIN for the purpose of the Companies Act, 2013.

Further, it is to be noted that “Director Identification Number” (DIN) shall include the Designated Partnership Identification Number (DPIN) issued under section 7 of the Limited Liability Partnership Act, 2008 and the rules made thereunder.

Example 7: Mr. Rajesh having DIN 00452568 and already appointed in Raj Industries Private Limited. Now, he wants to appoint himself in M/s. Karnawat Industries LLP as a designated partner.

⁴Explanation to Section 152 (7).

⁵As per Rule 2 (1) (e) of the Companies (Specification of Definitions Details) Rules, 2014

Here, he does not require to apply for DPIN. As per section 7 of the Limited Liability Partnership Act, 2008, DIN can be used as DPIN for Designated Partner.

Requirement of DIN: According to Section 152 (3), no person shall be appointed as a director of a company unless he has been allotted the Director Identification Number (DIN) under section 154 or any other number as may be prescribed under section 153.

Filing of Application for allotment of DIN: Section 153 deals with the filing of application for allotment of DIN. Accordingly, every individual intending to be appointed as director of a company shall make an application for allotment of DIN to the Central Government in the prescribed form and manner and along with prescribed fees.

It is provided that the Central Government may prescribe any identification number which shall be treated as Director Identification Number and in case any individual holds or acquires such identification number, the requirement of Section 153 shall not apply or apply in such manner as may be prescribed.

Further, Rule 9 of the Companies (Appointment and Qualifications of Directors) Rules, 2014 states the following **procedure** for making an **application for allotment of DIN before appointment in an existing company**:

- (1) **Filing of application** : Every applicant, who intends to be appointed as director of an existing company shall make an application electronically in Form DIR-3, to the Central Government⁶ for allotment of a Director Identification Number (DIN) along with the prescribed fees.

It is provided that in case of proposed directors not having DIN, the particulars of maximum three directors shall be mentioned in Form No. INC-32 (SPICe) and DIN may be allotted to maximum three proposed directors through Form INC-32 (SPICe).

Example 8- Mr. Varun, Mr. Ankit and Mr. Parag are planning to incorporate a private limited company. They do not have DIN because they are becoming directors in any company for the first time. Here, they can apply for allotment of DIN along with the form of incorporation of the Company i.e Form INC-32 (SPICe).

- (2) **Providing of electronic system to facilitate submission of application:** The Central Government shall provide an electronic system to facilitate submission of application for the allotment of DIN through the portal on the website of the Ministry of Corporate Affairs.
- (3) (a) **Filling of required information in Form attached with relevant documents:** The applicant shall download Form DIR-3 from the portal, fill in the required particulars

⁶Vide Notification No. S.O. 1354(E) dated 21st May, 2014, issued by MCA, the powers and functions of the Central Government in respect of allotment of Director Identification Number under Sections 153 and 154 stand delegated to the Regional Director, Joint Director, Deputy Director or Assistant Director posted in the office of Regional Director at Noida.

sought therein, verify and sign the form and after attaching copies of the following documents, scan and file the entire set of documents electronically-

- (i) photograph;
 - (ii) proof of identity;
 - (iii) proof of residence;
 - (iiia) board resolution proposing his appointment as director in an existing company
 - (iv) specimen signature duly verified.
- (b) **Submission of digitally signed Form:** Form DIR-3 shall be signed and submitted electronically by the applicant using his or her own Digital Signature Certificate and shall be verified digitally by a company secretary in full time employment of the company or by the managing director or director or CEO or CFO of the company in which the applicant is intended to be appointed as director in an existing company.
- (4) In case the name of a person does not have a last name, then his or her father's or grandfather's surname shall be mentioned in the last name along with the declaration in Form No.DIR-3A.

Allotment of DIN: According to section 154, the Central Government shall allot a Director Identification Number (DIN) to the applicant in the prescribed manner **within one month** from the receipt of application.

Rule 10 of the Companies (Appointment and Qualifications of Directors) Rules, 2014 provides the following **procedure** for rejection or allotment of DIN:

- (i) **Generation of application number-**On the submission of the Form DIR-3 on the portal and on payment of the requisite fees, an application number shall be generated by the system automatically.

Provided that no application number shall be generated in case of the person applying for Director Identification Number is a national of a country which shares land border with India, unless necessary security clearance from the Ministry of Home Affairs, Government of India has been attached alongwith application for Director Identification Number.

- (ii) **Communication of issue of DIN-**After generation of application number, the Central Government shall process the applications received for allotment of DIN and decide on the approval or rejection thereof and communicate the same to the applicant along with the DIN allotted in case of approval by way of a letter by post or electronically or in any other mode, within a period of **one month** from the receipt of such application.
- (iii) **In case of defective/incomplete application-**If the Central Government, on examination, finds such application to be defective or incomplete in any respect, it shall give intimation of such defect or incompleteness, by placing it on the website and by email to the applicant who

APPOINTMENT AND QUALIFICATIONS OF DIRECTORS

1.15

has filed such application. The applicant shall be directed to rectify the defects or incompleteness by resubmitting the application **within a period of 15 days** of such placing on the website and email.

It is provided that the Central Government shall –

- (a) reject the application and **direct the applicant to file fresh application** with complete and correct information, where the defect has been rectified partially or the information given is still found to be defective;
 - (b) **treat and label such application as invalid in the electronic record** in case the defects are not removed within the given time; and
 - (c) **inform the applicant** either by way of letter by post or electronically or in any other mode.
- (iv) In case of rejection or invalidation of application, the **fee so paid** with the application shall **neither be refunded nor adjusted** with any other application.

Note 1: All DINs allotted to individual(s) by the Central Government before the commencement of these rules shall be deemed to have been allotted to them under these rules.

Note 2: The DIN so allotted under these rules is valid for the life-time of the applicant and shall not be allotted to any other person.

Procedure for allotment of DIN

- On submission of Form and fees, application no. is generated on the system
- CG shall process such application
- approval or rejection is communicated to the applicant within 1 month from receipt of such application

in case of approval, DIN allotted will be sent through by post/electronically/in any other manner

In case of defective/incomplete application, CG shall place it on website and intimate by email to the applicant

- direct to rectify the defects/incompleteness by resubmitting the application within 15 days of placing on website and email.
- CG shall reject and direct to file fresh application, where defect rectified partially /information given is defective
- In case of non -removal of defect- treat and label as invalid in electronic records.
- inform applicant of rejection /invalidation and no-refund or adjustment of paid fees

Prohibition on obtaining more than one DIN: According to Section 155, no individual, who has already been allotted a DIN under section 154, shall apply for, obtain or possess another DIN.

Example 9: Mr. Tahir was appointed as a director in Bombay Textiles Private Limited with DIN 00658400. Now, He wants to be appointed as a director in another company. Here, Mr. Tahir shall have to use existing DIN for appointment as a director in new company. He can not apply for another DIN.

Director to intimate DIN: According to Section 156, every existing director shall, **within one month** of the receipt of DIN from the Central Government, intimate his DIN to the company or all the companies wherein he is a director.

Company to inform DIN to Registrar: According to section 157 (1), every company shall, **within 15 days** of the receipt of intimation under section 156, furnish the DIN of all its directors to the Registrar or any other officer or authority as may be specified by the Central Government with such fees or additional fees as may be prescribed. Every such intimation shall be furnished in the prescribed form and manner.

According to **Rule 10A** of the Companies (Appointment and Qualifications of Directors) Rules, 2014:

- (1) Every director, functioning as a director in one or more companies on or before the 30th June, 2007 and who has not yet intimated his DIN to such company or companies shall, within one month of the receipt of Director Identification Number from the Central Government, intimate his Director Identification Number to the company or all companies wherein he is a director as per Form DIR-3B.
- (2) The intimation by the company of Director Identification Number of its directors under section 157 shall be furnished in Form DIR-3C within 15 days of receipt of intimation under section 156.

Punishment for failure to furnish the DIN to Registrar: According to Section 157(2) if any company fails to furnish the DIN to Registrar, it shall be liable to a penalty as under:

- ₹ 25,000 and in case of continuing failure, with a further penalty of ₹ 100 for each day after the first during which such failure continues, subject to a maximum of ₹ 1,00,000.
- Further, every defaulting officer of the company shall be liable to a penalty as under:
Minimum penalty of ₹ 25,000 and in case of continuing failure, with a further penalty of ₹ 100 for each day after the first during which such failure continues, subject to a maximum of ₹ 1,00,000.

Obligation to indicate DIN: According to Section 158, every person or company, while furnishing any return, information or particulars as are required to be furnished under the Companies Act, 2013, shall mention the Director Identification Number in such return, information or particulars in case such return, information or particulars relate to the director or contain any reference of any director.

Punishment for contravention of Sections 152, 155 and 156: Section 159 provides that if any individual or director of a company makes any default in complying with any of the provisions of section 152, section 155 and section 156, such individual or director of the company shall be liable to a penalty as under:

- Penalty upto ₹ 50,000 and where the default is a continuing one, with a further penalty up to ₹ 500 for each day after the first during which such default continues.

Cancellation or Surrender or De-activation and Re-activation of DIN:

Rule 11 of the Companies (Appointment and Qualifications of Directors) Rules, 2014 lays down the procedure for cancellation or surrender or deactivation and re-activation of DIN as under:

- (1) The Central Government or Regional Director (Northern Region), Noida or any officer authorised by the Regional Director may, upon being satisfied on verification of particulars or documentary proof attached with the application received along with prescribed fee from any person, cancel or deactivate the DIN in case -

- (a) the **DIN is found to be duplicated** in respect of the same person provided the data related to both the DINs shall be merged with the validly retained number;
- (b) the **DIN was obtained in a wrongful manner** or by **fraudulent means**;

However, before cancellation or deactivation of DIN pursuant to the clause (b) above, an opportunity of being heard shall be given to the concerned individual.

For this purpose

- (i) the term **“wrongful manner”** means if the DIN is obtained on the strength of documents which are not legally valid or incomplete documents are furnished or on suppression of material information or on the basis of wrong certification or by making misleading or false information or by misrepresentation.
 - (ii) the term **“fraudulent”** means if the DIN is obtained with an intent to deceive any other person or any authority including the Central Government.
- (c) of the **death of the concerned individual**;
 - (d) the **concerned individual** has been **declared as a person of unsound mind** by a competent Court;
 - (e) if the **concerned individual** has been **adjudicated an insolvent**.
 - (f) **on an application** made in Form DIR-5 **by the DIN holder to surrender** his or her DIN along with declaration that he has never been appointed as director in any company and the said DIN has never been used for filing of any document with any authority, the Central Government may deactivate such DIN.

However, before deactivation of any DIN in the above case (f), the Central Government shall verify e-records.

- (2) The Central Government or Regional Director (Northern Region), or any officer authorised by the Central Government or Regional Director (Northern Region) shall, deactivate the Director Identification Number (DIN), of an individual who does not intimate his particulars in e-form DIR-3-KYC within the stipulated time in accordance with Rule 12A.

- (3) The de-activated DIN shall be re-activated only after e-form DIR-3 is filed along with the fee as prescribed under the Companies (Registration Offices and Fees) Rules, 2014.

Intimation of Changes in Particulars specified in DIN Application:

Rule 12 of the Companies (Appointment and Qualifications of Directors) Rules, 2014, provides for the following procedure for intimation of changes in particulars specified in the DIN application:

- (1) **Intimation of change to Central Government:** Every individual who has been allotted a DIN under these rules shall, in the event of any change in his particulars as stated in Form DIR-3, intimate such change(s) to the Central Government within a period of **thirty days** of such change(s) in Form DIR-6 in the following manner, namely:
 - (i) The applicant shall download Form DIR-6 from the portal, fill in the relevant changes, verify the form and attach duly scanned copy of the proof of the changed particulars and submit electronically;
 - (ii) the form shall be digitally signed by a chartered accountant in practice or a company secretary in practice or a cost accountant in practice;
 - (iii) the applicant shall submit the Form DIR-6;
- (2) **Applicant to be informed of change in the electronic database:** The Central Government, upon being satisfied, after verification of such changed particulars from the enclosed proofs, shall incorporate the said changes and inform the applicant by way of a letter by post or electronically or in any other mode confirming the effect of such change in the electronic database maintained by the Ministry.
- (3) **Intimation to concerned Registrar:** The DIN cell of the Ministry shall also intimate the change(s) in the particulars of the director submitted to it in Form DIR-6 to the concerned Registrar(s) under whose jurisdiction the registered office of the company(s) in which such individual is a director is situated.
- (4) **Individual to inform change in particulars to the company/ies:** The concerned individual shall also intimate the change(s) in his particulars to the company or companies in which he is a director **within 15 days** of such change.

In the decided case of *Imraj Ali Molla v. Union of India*, W.P. Nos. 268 and 273 of 2019 March 18, 2020, it was held that since DIN is allocated under section 154 and there is no provision in Act for deactivation of DIN of a director only on ground of disqualification under section 164(2)(a) or section 167(1)(a), action of RoC in deactivating DIN of petitioners on ground of such violation of section 164(2)(a) of a particular company could not confer a right on RoC to deactivate such DIN.

It was laid in *Gaurang Balvantlal Shah v. Union of India*, R/Special Civil Application Nos. 22435 of 2017 and Others, December 18, 2018, that DIN of a director cannot be cancelled or deactivated except under circumstances mentioned in rule 11 of Companies (Appointment of Directors) Rules, 2014.



5. RIGHT OF PERSONS OTHER THAN RETIRING DIRECTORS TO STAND FOR DIRECTORSHIP [SECTION 160]

A person who is not a retiring director is also eligible to stand for directorship. Section 160 of the Act and Rule 13 of the Companies (Appointment and Qualifications of Directors) Rules, 2014 contain provisions in this respect. These are discussed as under:

(i) Requirement of Written Notice:

- (a) **Person who applies his candidature as a director:** A person other than retiring director shall be eligible for appointment as a director in a company at any general meeting (Whether in AGM or EOGM), if he has given a notice in writing under his hand signifying his candidature as a director at least 14 days before the meeting at the registered office of the company.
- (b) **Member who intends to propose other person for directorship:** Instead of above person, some other member of the company who intends to propose such other person as a director can also give a written notice at the registered office of the company signifying his intention to propose the other person as a candidate for directorship at least 14 days before the meeting.

- (ii) **Requirement of Deposit:** The written notice needs to be accompanied with the deposit of ₹ 1,00,000 or such higher amount as may be prescribed.

Exceptions-The requirement of deposit shall not apply in following cases of directors

- Independent Director
- director recommended by the Nomination and Remuneration Committee, if any under section 178(1)
- director recommended by the Board of Directors, where there is no Nomination and Remuneration Committee.

- (iii) **Action by the company:** The company shall inform its members regarding the candidature of a person for the office of director in accordance with the manner prescribed in Rule 13 of the Companies (Appointment and Qualifications of Directors) Rules, 2014. The same is stated below:

At least 7 days before the general meeting, the company shall inform its members of such candidature-

- (1) **by serving individual notices** through electronic mode to such members who have provided their e-mail addresses for communication purposes and in writing to all other members; and
- (2) **by placing notice** of such candidature on its website, if any.

When there is no need to serve notices individually: It shall not be necessary for the company to serve individual notices if it **advertises such candidature**, not less than 7 days before the meeting:

- (a) at least once in a vernacular newspaper in the principal vernacular language of the district in which the registered office of the company is situated, and
- (b) at least once in English language in an English newspaper circulating in that district.

- (iv) **Refund of Deposit:** The amount of deposit shall be refunded to such person or, as the case may be, to the member, if the person proposed gets selected as a director or gets more than 25% of the total valid votes cast either on show of hands or on poll.

Explanation – No deposit fees shall be refunded to those candidates who are not appointed as directors or do not get more than 25% of total valid votes in favour of their appointment.

Note 1: For the purposes of Section 160, the expression 'retiring director' means a director retiring by rotation⁷.

Note 2: Not all the directors are retiring directors. Therefore, if an additional director or an alternate director or a nominee director or a director appointed to fill a casual vacancy, is to be appointed as a regular director at the general meeting, the procedure prescribed by Section 160 is required to be followed. Similarly, where a director retires by rotation but instead of re-appointing him, a new person in his place is proposed to be appointed, provisions of Section 160 are attracted.

Clarifications

(1) As per Notification No. G.S.R. 465(E), dated 5th June, 2015, in case of **Nidhis**, the amount of deposit for the purpose of Section 160(1) shall be **"ten thousand rupees"**. In other words, a person (not a retiring director) proposing his candidature as director in Nidhis or some other member proposing such person's candidature shall be required to deposit ₹ 10,000 along with the written notice.

(2) The MCA vide General Circular No. 38/2014, dated 14th October, 2014, has clarified that in case of **Section 8 companies**, their Board of Directors shall decide as to whether the deposit of ₹1,00,000 is to be forfeited or refunded if the person proposed as director fails to secure more than 25% of the valid votes.

⁷Explanation to Section 152 (7).

Exemptions

(1) In terms of Notifications No. 463 (E), dated 5th June, 2015, as amended by Notifications No. 582 (E), dated 13th June, 2017, **Section 160 shall not apply to:**

(a) **A Government company** in which the entire paid up share capital is held by the Central Government, or by any State Government or Governments or by the Central Government and one or more State Governments;

(b) **A subsidiary of a Government company**, referred to in (a) above, in which the entire paid up share capital is held by the Government company.

(2) In terms of Notifications No. 464 (E), dated 5th June, 2015 as amended by Notifications No. 583 (E), dated 13th June, 2017, similar exemption from Section 160 is applicable to a **private company**.

(3) In terms of Notifications No. 466 (E), dated 5th June, 2015 as amended by Notifications No. 584 (E), dated 13th June, 2017, similar exemption from Section 160 is also applicable to **Section 8 companies** whose articles provide for election of directors by ballot.

Note: In all the three cases mentioned above exemption from the application of Section 160 is available only if the concerned company has not committed a default in filing its financial statements under Section 137 or Annual return under Section 92 with the Registrar.



6. APPOINTMENT OF DIRECTOR ELECTED BY SMALL SHAREHOLDERS [SECTION 151]

According to Section 151 of the Act, a listed company may have one director elected by the small shareholders. This provision enables the small shareholders to place their representative on the Board of Directors of a listed company so that their voice is also listened effectively.

The term “**small shareholders**” means a shareholder holding shares of nominal value of not more than 20,000 or such other sum as may be prescribed.

Manner of appointment of small shareholders’ director and terms and conditions of such appointment are prescribed by Rule 7 of the Companies (Appointment and Qualifications of Directors) Rules, 2014. These provisions are discussed below:

(i) **Strength of Small Shareholders required for appointment of their Director:** A listed company may, upon notice of not less than:

(a) one thousand small shareholders; or

(b) 1/10th of the total number of such shareholders,

whichever is lower

have a small shareholders’ director elected by the small shareholders.

However, a listed company may opt to have a director on suo moto representing small shareholders and in such a case the provisions given below in Point (ii), shall not apply for appointment of such director.

- (ii) **Serving of notice by small shareholders:** The small shareholders intending to propose a person as a candidate for the post of small shareholders' director shall give a notice of their intention with the company **at least fourteen days** before the meeting under their signature specifying the name, address, shares held and folio number of the person whose name is being proposed for the post of director and of the small shareholders who are proposing such person for the office of director.

However, if the person being proposed does not hold any shares in the company, the details of shares held and folio number need not be specified in the notice.

- (iii) **Statement to be annexed with notice:** The notice shall be accompanied by a statement signed by the person whose name is being proposed for the post of small shareholders' director stating-

- (a) his Director Identification Number (DIN);
- (b) that he is not disqualified to become a director under the Act; and
- (c) his consent to act as a director of the company.

- (iv) **Small shareholders' director as independent director:** Such director shall be considered as an independent director. Therefore, he should meet the eligibility criteria pertaining to independent director as given under section 149(6) and should give a declaration of his independence in accordance with section 149(7) of the Act.

- (v) **Applicability of section 152:** The appointment of small shareholders' director shall be subject to the provisions of section 152 **except that-**

- (a) such director shall not be liable to retire by rotation;
- (b) such director's tenure as small shareholders' director shall not exceed a period of **three consecutive years**; and
- (c) on the expiry of the tenure, such director shall not be eligible for re-appointment.

- (vi) **Applicability of Section 164:** A person shall not be appointed as small shareholders' director of a company, if he is not eligible for appointment in terms of section 164 which specifies the disqualifications for appointment as a director.

- (vii) **Vacation of office:** A person appointed as small shareholders' director shall vacate the office if -

- (a) the director incurs any of the disqualifications specified in Section 164;

- (b) the office of the director becomes vacant in pursuance of Section 167⁸;
- (c) the director ceases to meet the criteria of independence as provided in Section 149 (6).
- (viii) **Maximum number of directorships:** No person shall hold the position of small shareholders' director in more than two companies at the same time.

However, the second company in which he has been so appointed shall not be in a business which is competing or is in conflict with the business of the first company.

- (ix) **Cooling period:** A small shareholders' director shall not be appointed in or be associated with such company in any other capacity, either directly or indirectly for a period of **three years** from the date on which he ceases to hold office as a small shareholders' director in a company.



7. APPOINTMENT OF ADDITIONAL DIRECTOR, ALTERNATE DIRECTOR, A DIRECTOR TO FILL CASUAL VACANCY AND NOMINEE DIRECTOR [SECTION 161]

- (A) **Additional Director [Section 161(1)]:** According to the section:

- (i) The articles of a company may confer on its Board of Directors the power to appoint any person as an additional director at any time.
- (ii) A person, who fails to get appointed as a director in a general meeting, cannot be appointed as an additional director.
- (iii) Additional director shall hold office up to the date of the next annual general meeting or the last date on which the annual general meeting should have been held, whichever is earlier.

With a view to meet urgent requirements of management, the Board of Directors is empowered to appoint any person as an additional director at any time if such power is granted by the articles. **The notable point is that it is not Section 161 (1) but the articles which confer such power.**

The person to be appointed as additional director should possess DIN and must not be the person who failed to get appointed in a general meeting. This brings to the force the power of shareholders *i.e.* any person discarded as director at a general meeting by the shareholders cannot get appointed by the Board of Directors through back-door entry.

⁸ Section 167 of the Act specifies various grounds, which if attracted, shall make a director liable to vacate his office.

Further, an additional director is not a retiring director. Therefore, his appointment as regular director requires that the provisions of Section 160 are followed.

Term of office of additional director: The term of additional director is limited to the holding of ensuing Annual General Meeting (AGM). Even if the AGM is not held on the last due date, the term ends there itself and it cannot be extended to a date when the AGM, in actuality, shall be held in future after its due date.

(B) Alternate Director [Section 161(2)]: According to this section:

- (i) The Board of Directors of a company may, **if so authorised by its articles or by a resolution passed by the company in general meeting**, appoint a person, not being a person holding any alternate directorship for any other director in the company or holding directorship in the same company, to act as an alternate director for a director during his absence for a period of **not less than three months** from India.
- (ii) No person shall be appointed as an alternate director for an independent director unless he is qualified to be appointed as an independent director under the provisions of this Act.
- (iii) An alternate director shall not hold office for a period longer than that permissible to the original director in whose place he has been appointed and shall vacate the office if and when the original director returns to India.
- (iv) If the term of office of the original director is determined before he so returns to India, any provision for the automatic re-appointment of retiring directors in default of another appointment shall apply to the original, and not to the alternate director.

The power to appoint an alternate director rests with the Board of Directors. However, such power must be conferred by the articles or by a resolution passed at the general meeting.

An alternate director is appointed in place of a regular director who has gone out of India. The period of absence of such original director from India must be minimum three months or more. A short absence of less than three months does not entitle the Board to appoint an alternate director. Such proposed alternate director should possess DIN.

A person selected for appointment as alternate director must not be the one who is holding any alternate directorship for any other director in the company. In other words, a person who is already an alternate director in the company cannot hold another alternate directorship in that company. Further, the selected person must also not be a director in the same company. Thus, a person already a director cannot at the same time be an alternate director in the same company but a person holding directorship in any other company can be considered for the appointment as alternate director. However, for considering maximum number of directorships of a person under Section 165, the alternate directorship shall also be counted. Thus, a fresh alternate directorship should be taken up by the person concerned only if his

holding of regular as well as alternate directorships does not exceed the maximum limit. Further, he should not be disqualified to hold the office of a director.

Example 10: Mr. Devendra Kumar has been appointed as an alternate director in place of Mr. Gaurav Jain (i.e. Original Director) in Urban Development Private Limited. Now, company wants to appoint Mr. Devendra Kumar as an alternate director in place of Ms. Shaily Jaiswal (i.e. another original director of the same company).

Here, Mr. Devendra cannot be appointed as an alternate director of another original director of the company.

In case, the original director is an independent director and he leaves for a place outside India for three months or more, the person who is to be appointed in his place as alternate director must be qualified to be appointed as an independent director. In other words, the status of independence as well as other requisites of an independent director must form part of such alternate director who is selected for appointment in the absence of an independent director.

A 'would be alternate director' is not exempted from furnishing his consent to act as director. Therefore, he must furnish his consent in DIR-2 to the company on or before his appointment and in turn the company shall file his consent with the Registrar in DIR-12.

Term of office of alternate director: The term of office of an alternate director coincides with the permissible term applicable to the original director in whose place he has been appointed. Thus, the term shall not be longer than the term which is permissible to the original director; and as soon as the original director ceases to be a director (death included) the alternate director follows his steps and is required to vacate the office. Further, the alternate director shall vacate the office immediately on the return of original director to India.

It may happen that the term of original director expires while he is still outside India. In such a case, the provisions relating to automatic deemed re-appointment as envisaged in Section 152 (7) (b) shall apply to the original director and not to the alternate director appointed in his place. Thus, the original director (and not alternate director) shall be deemed as re-appointed at the adjourned AGM if the company does not appoint another person on the expiry of the term of original director.

Appointment of alternate director by original director: The original director who is leaving to a place outside India cannot appoint an alternate director in his place. It is the Board which shall make the appointment because the authority for such appointment vests in the Board. Following example will make the situation clear:

Example 11: Mr. Q, a Director of PQR Limited proceeding on a long foreign tour (period of duration outside India exceeded three months), appointed Mr. Y as an alternate director to act for him during his absence. The articles of the company provide for appointment of alternate directors. Mr. Q claims that he has a right to appoint alternate director.

As per section 161(2), the Board of Directors of a company may, if so authorised by its articles or by a resolution passed by the company in general meeting, appoint a person, not being a person holding any alternate directorship for any other director in the company or holding directorship in the same company, to act as an alternate director for a director during his absence for a period of not less than three months from India. From the above provision it is clear that the authority to appoint alternate director has been vested in the Board of Directors only and that too subject to empowerment by the articles or by a resolution passed by the company in general meeting.

Therefore, Q, in this case is not authorized to appoint an alternate director and the appointment of Mr. Y is not valid.

(C) Nominee Director [Section 161(3)]: According to this section:

‘Subject to the articles of a company, the Board may appoint any person as a director nominated by any institution in pursuance of the provisions of any law for the time being in force or of any agreement or by the Central Government or the State Government by virtue of its shareholding in a Government company.’

Simply stated, a nominee director is not like any other director. He represents the body which makes his nomination for appointment as director in the company. Whenever a company obtains financial assistance from some financial institution or bank, such institution invariably nominates its representative for safeguarding its interests till the loaned amount is completely repaid. The nominee director is expected to ensure that the terms of loan agreements are religiously complied with all the time by the company concerned which has been granted financial assistance. The Board of Directors (subject to the articles) is empowered to appoint a nominee director and the shareholders cannot interfere with such appointment. Further, by virtue of its shareholding in a Government company, the Central Government or the State Government may also nominate a person for appointment as nominee director and the Board shall have to follow the suit without any hinderance on its part.

(D) Casual Vacancy [Section 161(4)]: According to this section:

- (i) if the office of any director appointed by the company in general meeting is vacated before his term of office expires in the normal course, the resulting casual vacancy may, in default of and subject to any regulations in the articles of the company, be filled by the Board of Directors at a meeting of the Board which shall be subsequently approved by members in the immediate next general meeting.
- (ii) Any person so appointed shall hold office only up to the date up to which the director in whose place he is appointed would have held office if it had not been vacated.

The above provisions are discussed as under:

The term 'casual' means a sudden happening *i.e.* something which happened by chance or unexpectedly or unforeseen but not by efflux of time. A casual vacancy results when the office of any director appointed in the general meeting is vacated before the expiry of his term in the normal course. This is not the vacancy created due to the retirement of a director. It is created because of certain other factors that are not linked with retirement like occurrence of death or attraction of disqualification or tendering of resignation or removal, etc. Further, in this case, the term of the office of director because of which the casual vacancy is created does not get expired in the normal course.

A vacancy which was created due to the fact that the elected director declined to assume the office after his appointment at general meeting cannot be said to result in a casual vacancy. In such a case, when there was no assume of office by the director, how can he vacate it. Thus, there arises no casual vacancy.

Section 161 (4) does not require that articles should expressly empower the Board of Directors for filling a casual vacancy. When a casual vacancy occurs it shall be filled by the Board at its meeting by passing a resolution and not otherwise. The vacancy so filled by the Board shall be approved subsequently by members in the immediate next general meeting. It is to be noted that where articles contain any regulations as regards filling of casual vacancy they need to be followed by the Board; but the subsequent approval of such filling of vacancy by members in the immediate next general meeting is a must.

As we have noticed, the casual vacancy arises when any director appointed in the general meeting vacates his office before the expiry of his term. Thus, such appointment of the director who vacates his office must have been made in the general meeting and when the casual vacancy is filled by the Board and subsequently approved by the members in the immediate next general meeting, the matter ends there. Subsequently, if the casual vacancy so filled is again vacated due to some casual occurrence, then it cannot be said to be a casual vacancy because it arose against an appointment which was not made in the general meeting. Such type of vacancy needs to be filled by the Board by appointing an additional director.

A director appointed to fill a casual vacancy is not a 'casual director'. He enjoys all the powers as well as is required to bear the responsibilities of the director in whose place he is appointed except that where the earlier director was an 'interested director', his 'interest' cannot be attached to the new director filling the casual vacancy.

In case a company has appointed a woman director because of statutory requirement and an intermittent vacancy is created in the office of such woman director, the Board shall fill such casual vacancy at the earliest but not later than immediate next Board meeting or three

months from the date of creation of such vacancy, whichever is later.⁹ Similar is the case with an independent director whose intermittent vacancy must be filled at the earliest but not later than immediate next Board meeting or three months from the date of occurrence of such vacancy, whichever is later.¹⁰ However, there is no such urgency so far as filling of any other casual vacancy is concerned (i.e. not of a woman director or of an independent director) because if the Board of Directors feels that the affairs of the company can be managed without appointing anybody, then the Board can postpone such appointment.

Term of office of a director appointed to fill a casual vacancy: The term of office of a director appointed to fill a casual vacancy continues till such time up to which the term of the director because of whom the casual vacancy was created would have continued. Thus, the person filling the casual vacancy shall hold office up to the date up to which the director in whose place he is appointed would have continued in the office which in other words means 'up to the unexpired term of such director'. The 'continuation clause' is applicable because of the Proviso mentioned under Section 161 (4); but for the application of this 'continuation clause' the appointment made by the Board needs to be approved by the members in the immediate next general meeting.



8. APPOINTMENT OF DIRECTORS TO BE VOTED INDIVIDUALLY [SECTION 162]

Section 162 of the Companies Act prohibits appointment of directors by passing a single resolution. Electing more than one person as directors through a single resolution deprives the shareholders from exercising their choice to reject a specific individual. In such a situation, either they will have to vote against or in favour of all the prospective directors i.e. it shall be difficult for them to reject a particular person as director unless they reject such resolution *in toto*, thus not appointing all the persons specified in that resolution. That is why, Section 162 requires every individual person to be voted individually for appointment as director. As stated in the box below, if certain conditions are satisfied this provision shall not apply to a Government company and its wholly-owned subsidiary. Further, a private company is also exempted from this provision.

In nutshell, provisions of Section 162 are as under:

- (i) Two or more directors of a company cannot be elected as directors by a single resolution. It implies that **each person shall be appointed as director by a separate resolution.**

⁹As per Second Proviso to Rule 3 of the Companies (Appointment and Qualifications of Directors) Rules, 2014.

¹⁰As per Second Proviso to Rule 4 (1) of the Companies (Appointment and Qualifications of Directors) Rules, 2014.

- (ii) As an **exception**, two or more persons can be appointed as directors by a single resolution if a proposal to move such a resolution (*i.e.* appointing two or more persons as directors by a single resolution) has first been **agreed to at the general meeting without any vote being cast against it**.

Example12: A company held its general meeting at its registered office with twenty members present. At the meeting a proposal was moved to appoint three persons as directors by a single resolution. This proposal was agreed to by the seventeen shareholders who voted in its favour but the remaining three members did not vote at all. Thus, no vote was cast against the proposal. In such a situation, the company can appoint three persons as directors by a single resolution. Such single resolution shall be passed by simple majority *i.e.* as an ordinary resolution.

- (iii) A resolution moved in contravention of the provision stated in point (ii) above shall be void, whether or not objection thereto was raised at the time when it was so moved.
- (iv) A motion for approving a person for appointment, or for nominating a person for appointment as a director, shall be treated as a motion for his appointment.

Exemptions

Non-applicability of Section 162 of the Act of 2013:

(1) Notifications No. GSR 463(E), dated 5th June, 2015 as amended by Notification No. GSR 582 (E), dated 13-06-2017 states that Section 162 requiring appointment of each person as director by a separate resolution, shall not apply to:

- (a) **A Government company** in which the entire paid up share capital is held by the Central Government, or by any State Government or Governments or by the Central Government and one or more State Governments;
- (b) **A subsidiary of a Government company**, referred to in (a) above, in which the entire paid up share capital is held by that Government company.

However, above exemption is applicable only if such Government company has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar.

(2) Similarly, Notifications No. and 464(E), dated 5th June, 2015 as amended by Notification No. GSR 583 (E), dated 13-06-2017 exempts a **private company** from the application of Section 162. However, this exemption is applicable only if such private company has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar.



9. OPTION TO ADOPT PRINCIPLE OF PROPORTIONAL REPRESENTATION FOR APPOINTMENT OF DIRECTORS [SECTION 163]

As a general rule, the directors in a company are appointed by simple majority. It implies that the shareholders having voting rights just equal to 51 percent can easily negate the choice of other minority shareholders who have substantial voting rights as high as up to 49 percent in the matter of appointment of directors. Thus, minority shareholders though having sizeable voting rights may not find it possible to appoint even a single director of their own on the Board of Directors. To counter this kind of unpleasant situation which may create confrontation in a company and adversely affect the managerial efficiency. Section 163 chalks out a system by which directors may be appointed by way of proportional representation. The provisions of Section 163 are stated as under:

- (i) Section 163 starts with the phrase 'Notwithstanding anything contained in this Act' which implies that **this section has overriding effect** i.e. it overrides all other provisions of the Companies Act, 2013.
- (ii) The **articles of a company need to contain provisions** for the appointment of directors by proportional representation. The procedure as contained in the articles must be capable enough to enable the minority shareholders to have a proportionate representation on the Board of Directors.
- (iii) The articles need to provide **for the appointment of not less than two-third** (i.e. minimum $\frac{2}{3}$ rd or more) of the total number of the directors in accordance **with the principle of proportional representation**.
- (iv) Such appointments to be made in accordance with the principle of proportional representation, may use **following methods of voting**:
 - (a) Voting according to the **single transferable vote**. It means, a candidate gets elected if he secures the requisite votes fixed as quota; or
 - (b) Voting according to a system of '**cumulative voting**'; or
 - (c) **Otherwise i.e. adoption of any other transparent and effective method of voting** if it ensures that the Board shall have fair representation of the minority interest, in case methods stated at (a) or (b) are not adopted.
- (v) Such appointments may be made once in every **3 years**.
- (vi) **Casual vacancies of such directors shall be filled as provided in Section 161 (4) i.e.** such casual vacancy shall be filled as per the provisions of the articles; and if there is no such provision, then the Board of Directors may fill the vacancy through a board resolution. Later on, such appointment may be regularized by the shareholders at the immediately held general meeting.

Exemptions

Non applicability of Section 163: Section 163 of the Act, shall not apply to:

- (1) A **Government company** in which the entire paid up share capital is held by the Central Government, or by any State Government or Governments or by the Central Government and one or more State Governments;
- (2) A **subsidiary of a Government company**, referred to in (1) above, in which the entire paid up share capital is held by that Government company.

subject to the condition that such Government company has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar.

[Notifications No.GSR 463(E), dated 5th June, 2015 as amended by Notification No. GSR 582 (E), dated 13-06-2017]



10. DISQUALIFICATIONS FOR APPOINTMENT OF DIRECTOR [SECTION 164]

Section 164 of the Companies Act, 2013 contains disqualifications of a director. A person shall not be eligible for appointment as a director of a company if he suffers from any of the specified disqualifications. As such, the law does not specify any professional or educational qualifications of a director or requires him to hold requisite number of qualification shares except that as a general rule, any person desiring to become a director should be competent to contract and should have been allotted a Director Identification Number (DIN).

Various disqualifications are mentioned as under:

- (i) Section 164(1) states that a person shall not be appointed as a director if:
 - (a) he is of **unsound mind** and stands so declared by a competent court;
 - (b) he is an **undischarged insolvent**;
 - (c) he has **applied to be adjudicated as an insolvent and his application is pending**;
 - (d) he has been **convicted** by a court of any offence, whether involving moral turpitude or otherwise, and **sentenced to imprisonment for not less than 6 months** and a period of **5 years has not elapsed** from the date of expiry of the sentence.

However, in case a person has been convicted of any offence and sentenced in respect thereof to **imprisonment for a period of 7 years or more**, he shall not be eligible to be appointed as a director in any company

- (e) an **order disqualifying** him for appointment as a director has been passed by a court or Tribunal and the **order is in force**;

- (f) he has **not paid any calls** in respect of any shares of the company held by him and **6 months have elapsed** from the last day fixed for the payment of the call. It is immaterial whether such shares are held individually by him or jointly with others;
 - (g) he has been **convicted of the offence of dealing with related party transactions** under section 188 at any time **during the last preceding 5 years**; or
 - (h) he has **not complied with section 152 (3)** which requires a director to have a Director Identification Number (DIN).
 - (i) he has **not complied with the provisions of Section 165 (1)** relating to holding of specified number of directorships.
- (ii) Sub-section (2) of Section 164 prescribes **disqualifications which get attached to a person if he is or has been a director of a company which has committed default** as under—
- (a) his company has **not filed financial statements or annual returns** for any continuous period of **3 financial years**; or
 - (b) his company has **failed to repay the deposits** accepted by it or **pay interest** thereon or **to redeem any debentures** on the due date or **pay interest due thereon** or **pay any dividend declared** and **such failure** to pay or redeem **continues for 1 year or more**.

In both the above cases of default, the director concerned shall not be eligible to be re-appointed as a director of such defaulting company or appointed in some other company for period of 5 years from the date on which the said company has committed default.

Where a person is appointed as a director in a defaulted company: However, in case a person is appointed as a director of a company which has committed default as per clause (a) or clause (b) above, he **shall not incur** the disqualification for a period of **six months from the date of his appointment**.

Exemptions

*As per Notification No. GSR 463 (E), dated 5th June, 2015 as amended by Notification No. GSR 582 (E), dated 13th June, 2017, Section 164(2) is not applicable to a **Government company** provided it has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar.*

- (iii) **Additional qualifications by private company:** According to Section 164 (3), a private company (not being a subsidiary of a public company) is permitted to provide for additional disqualifications through its articles for appointment of a person as a director besides those specified in sub-sections (1) and (2) of section 164. [refer points (i) and (ii) above]. Thus, it may specify certain qualifications like a graduate shall only be the director or the prospective director should hold certain number of qualification shares, etc.

Note: In terms of Proviso to Section 164 (3), the disqualifications referred to in clauses (d), (e) and (g) of sub-section (1) shall continue to apply even if the appeal or petition has been filed against the order of conviction or disqualification.

- (iv) **Disqualification as prescribed by Section 217 (6)(ii):** Section 217 relates to a company which is under investigation. In case any director of such a company has been convicted of an offence under Section 217, the director shall be deemed to have vacated his office on and from the date on which he is so convicted. On such vacation of office, he shall be disqualified from holding an office in any company.

In Manju Chamundeeswari v. Union of India, W.M.P. NOS. 28025 & 28027 of 2021, it was laid that in terms of rule 11 of Companies (Appointment and Qualifications of Directors) Rules, 2014 neither cancellation nor deactivation of DIN is provided for upon disqualification under section 164(2) and such deactivation would be contrary to section 164(2), read with section 167(1) inasmuch as person concerned would continue to be a director of defaulting company.

The High Court of Kerala held in *Zacharia Maramkandathil Mohan v. Union of India* W.P (C) No. 21628 of 2020, June 16, 2021 the following principles :

- (i) Section 164(2) disqualifying directors of companies for a period of 5 years on failure to submit annual returns/financial statements for 3 consecutive years is not ultra vires Article 14 or Article 19(1)(g) of Constitution .
- (ii) Section 164(2) which had come into force from 1-1-2014 would have prospective and not retrospective effect and defaults contemplated under section 164(2)(a) with regard to non-filing of financial statements or annual returns for any continuous period of three financial years to be counted from financial year 2014-15 only.
- (iii) Disqualification under section 164(2) is of temporary nature, thus, rule 11 of Companies (Appointment and Qualifications of Directors) Rules, 2014 does not empower any authority to cancel or deactivate DIN upon disqualification under section 164(2).



11. MAXIMUM NUMBER OF DIRECTORSHIPS[SECTION 165]

Section 165 of the Act provides for the maximum permissible directorships that a person can hold. The provisions are as under:

- (i) **Maximum number of directorships:** According to Section 165(1), a person, after the commencement of the Companies Act, 2013, shall not hold office as director, including any alternate directorship, in more than 20 companies at the same time.

Further, out of the above limit of 20 companies, the maximum number of public companies in which a person can be appointed as a director shall not exceed 10.

It may be noted that the limit of public companies (i.e. 10) shall include directorship in private companies that are either holding or subsidiary company of a public company.

However, the limit of directorships of 20 companies shall not include the directorship in a dormant company; as also in a Section 8 company (refer Exemption mentioned in the box below).

Exemptions

Section 165(1) [refer point no.(i) above] shall not apply to a **Section 8 company** subject to the condition that such a company has not committed a default in filing its financial statements under Section 137 or Annual return under Section 92 with the Registrar. In other words, a directorship in a Section 8 company shall not be counted for determining the maximum permissible limit.

[Notification No. 466 (E), dated 5th June, 2015 as amended by Notification No. 584 (E), dated 13th June, 2017].

- (ii) **Lesser number of directorships than maximum:** The members of a company may, by **special resolution**, specify any lesser number of companies in which a director of the company may act as directors. [Section 165(2)]
- (iii) **Prescription of Transition Period of One Year:** Immediately before the commencement of the Companies Act, 2013 (i.e. before 01-04-2014), if a person was holding office as director in more companies than the specified limits, he was required, within one year (i.e. by 31-03-2015) to:
 - (a) choose not more than the specified limit of companies, in which he wished to continue to hold the office of director;
 - (b) resign his office as director in the other remaining companies; and
 - (c) intimate the choice made by him to each of the companies in which he was director and to the jurisdictional Registrar. [Section 165(3)]

Any resignation so made was to become effective immediately on the dispatch thereof to the company concerned. [Section 165(4)]

After dispatching the resignation of his office as director/non-executive director or after the completion of the transition period of one year (i.e. after 31-03-2015), whichever was earlier, no such person would act as director in more than the specified number of companies. [Section 165(5)]

In other words, after the completion of transition period of one year on 31-03-2015, no person is permitted to hold more directorships than the maximum specified.

- (iv) **Punishment for Contravention:** According to Section 165(6), if a person accepts an appointment as a director in contravention of Section 165(1) i.e. holding directorship of more than 20 companies or more than 10 public companies (subject to the exemptions, if any), he

shall be liable to a penalty of two thousand rupees for each day after the first during which such violation continues, subject to a maximum of two lakh rupees.



12. INDEPENDENT DIRECTORS

The legal provisions regarding independent directors are discussed below:

(a) **Number of Independent Directors:** Following companies are required to appoint specified number of independent directors:

(i) **Listed Companies:** Every listed public company shall have **at least one-third** of the total number of directors as independent directors. [Section 149(4)]

Note: Any fraction contained in such 1/3rd number shall be rounded off as one.

(ii) **Other Public Companies:** The Central Government is empowered to prescribe certain minimum number of independent directors in case of any class or classes of public companies. Taking a step in this direction, Rule 4(1) of the Companies (Appointment and Qualifications of Directors) Rules, 2014 has been framed which states that the following class or classes of companies shall have **at least two directors** as independent directors:

(1)	all such public companies which have paid up share capital of 10 crore rupees or more; or
(2)	all such public companies which have turnover of 100 crore rupees or more; or
(3)	all such public companies which have, in the aggregate, outstanding loans, debentures and deposits, exceeding 50 crore rupees.

Requirement of higher number: Due to composition of its audit committee, if a public company covered under the above rule, is required to appoint a higher number of independent directors, such higher number of directors shall be applicable to it.

As per section 177(2) of Act, the Audit Committee shall consist of a minimum of three directors with independent directors forming a majority.

Intermittent vacancy of an independent director: Any intermittent vacancy of an independent director shall be filled-up by the Board at the earliest but not later than **immediate next Board meeting or three months** from the date of such vacancy, whichever is later.

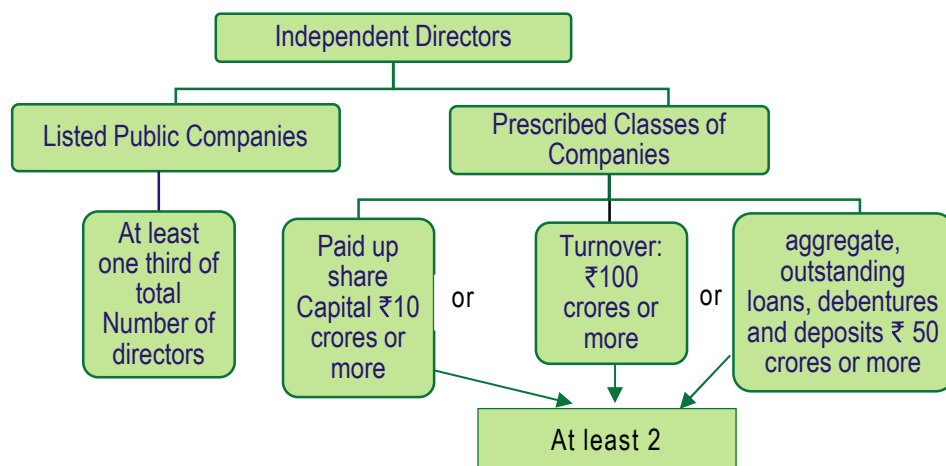
Duration of conditions after non-fulfilment of which no appointment required: A company which was obligated to appoint independent directors, shall not be required to make such appointment if it ceases to fulfill any of the three conditions relating to paid-up share

capital or turnover or outstanding loans, etc. [as laid down above in Rule 4(1)] for **three consecutive years**. It shall again be required to appoint independent directors if it starts meeting any of such conditions.

Clairification: Explanation to Rule 4 (1) clarifies that the paid up share capital or turnover or outstanding loans, debentures and deposits, as the case may be, as existing on the last date of latest audited financial statements shall be taken into account.

Exempted classes of unlisted public companies: According to Rule 4(2), following classes of unlisted public companies shall not be covered under sub-rule (1) of Rule 4:

- (a) a joint venture;
- (b) a wholly owned subsidiary; and
- (c) a dormant company as defined under section 455 of the Act.



If due to composition of audit committee any higher number of independent directors are required, such higher number shall be applicable.

Appointment of independent directors not required: If company ceases to fulfil any of the 3 conditions with respect to requirement of Paid up share capital, Turnover or of aggregate outstanding loans, debentures and deposits for 3 consecutive years.

Joint ventures, wholly owned subsidiaries and dormant companies are not covered under Rule 4 (1) which mentions about mandatory appointment of independent directors.

APPOINTMENT AND QUALIFICATIONS OF DIRECTORS

1.37

(b) **Who can become the Independent Director [Section 149(6)]:** In relation to a company, an independent director means a director (other than a managing director or a whole-time director or a nominee director¹¹), and who fulfills the following criteria:

- (1) who, in the opinion of the Board, is a person of **integrity** and possesses relevant **expertise and experience**;

Exemptions

*As per Notification No. G.S.R. 463 (E) dated 5th June, 2015, in case of a **Government company**, the word "Board" shall be substituted by the words "Ministry or Department of the Central Government which is administratively in charge of the company, or, as the case may be, the State Government"¹².*

- (2)
 - (A) who is or was not a promoter of the company or its holding, subsidiary or associate company;
 - (B) who is not related to promoters or directors in the company, its holding, subsidiary or associate company;
- (3) who has or had **no pecuniary relationship**, other than remuneration as such director or **having transaction not exceeding 10%** of his total income or such amount as may be prescribed, with the company, its holding, subsidiary or associate company, or their promoters, or directors, during the 2 immediately preceding financial years or during the current financial year;

Clarifications issued by MCA

(i) As regards '**pecuniary interest in certain transactions**', the MCA *vide* its General Circular No. 14/2014, dated 09-06-2014 has clarified that in case a transaction entered into by an independent director with the company concerned is at par with any member of the general public and at the same price as is payable/paid by such member of public, **it would not attract the bar of 'pecuniary relationship' under Section 149(6)(c) and therefore, an independent director will not be said to have 'pecuniary relationship' under this Section**, in such cases. This clarification has been issued by the MCA considering the provisions of Section 188 which take away transactions in the ordinary course of business at arm's length price from the purview of related party transactions.

¹¹As per *Explanation* to section 149(7), "**Nominee director**" means a director nominated by any financial institution in pursuance of the provisions of any law for the time being in force, or of any agreement, or appointed by any Government, or any other person to represent its interests.

¹²As per amendment Notification No. GSR 582 (E), dated 13-06-2017, the exceptions, modifications and adaptations mentioned in Notification No. GSR 463 (E), dated 05-06-2015 are applicable to such Government Company which has not committed a default in filing its financial statements under Section 137 or Annual return under Section 92 with the Registrar.

(ii) Further, vide above-referred General Circular, it is also clarified after consultation with SEBI that '**pecuniary relationship**' does not include (a) receipt of remuneration from one or more companies by way of fee provided under Section 197 (5); (b) reimbursement of expenses for participation in the Board and other meetings; and (c) profit related commission approved by the members, in accordance with the provisions of the Companies Act, 2013.

Exemptions

*As per Notification No. 463 (E), dated 5th June, 2015 as amended by Notification No. 582 (E), dated 13-06-2017, Point No. (3) mentioned above [i.e. Section 149(6)(c)] shall not apply in case of a **Government company** if it has not committed a default in filing its financial statements under Section 137 or Annual return under Section 92 with the Registrar.*

(4) none of whose relatives—

(i) in the company, its holding, subsidiary or associate company during the **2 immediately preceding financial years** or during the current financial year.

However, the relative may hold security or interest in the company of face value not exceeding fifty lakh rupees or two per cent of the paid-up capital of the company, its holding, subsidiary or associate company or such higher sum as may be prescribed;

(ii) **is indebted** to the company, its holding, subsidiary or associate company or their promoters, or directors, in excess of such amount as prescribed under Sub-rule 2 of Rule 5 (i.e., Rs. 50 Lakhs) of the Companies (Appointment and Qualifications of Directors) Rules, 2014 during the 2 immediately preceding financial years or during the current financial year;

(iii) has given a **guarantee** or provided any **security** in connection with the indebtedness of any third person to the company, its holding, subsidiary or associate company or their promoters, or directors of such holding company, for such amount as may be prescribed under Sub-rule 2 of Rule 5 (i.e., ₹ 50 Lakhs) of the Companies (Appointment and Qualifications of Directors) Rules, 2014 during the 2 immediately preceding financial years or during the current financial year; or

(iv) **has any other pecuniary transaction or relationship** with the company, or its subsidiary, or its holding or associate company amounting to **2% or more** of its gross turnover or total income singly or in combination with the transactions referred to in sub-clause (i), (ii) or (iii);

- (5) **who, neither himself nor any of his relatives—**
- (A) holds or has held the position of a **key managerial personnel** or is or has been **employee** of the company or its holding, subsidiary or associate company in any of the **3 financial years** immediately preceding the financial year in which he is proposed to be appointed;
 However, in case of a relative who is an employee, **the restriction under this clause shall not apply for his employment during preceding 3 financial years;**
 - (B) **is or has been an employee or proprietor or a partner**, in any of the 3 financial years immediately preceding the financial year in which he is proposed to be appointed, of—
 - (i) **a firm of auditors or company secretaries in practice or cost auditors** of the company or its holding, subsidiary or associate company; or
 - (ii) **any legal or a consulting firm** that has or had any transaction with the company, its holding, subsidiary or associate company amounting to **10% or more** of the gross turnover of such firm;
 - (C) holds together with his relatives **2% or more of the total voting power** of the company; or
 - (D) is a **Chief Executive or director**, by whatever name called, of any non- profit organisation that receives **25% or more** of its receipts from the company, any of its promoters, directors or its holding, subsidiary or associate company or that holds **2% or more of the total voting power** of the company; or
- (6) who possesses such **other qualifications** as are prescribed under Rule 5 of the Companies (Appointment and Qualifications of Directors) Rules, 2014 i.e.:
- (a) An independent director shall possess appropriate skills, experience and knowledge in one or more fields of finance, law, management, sales, marketing, administration, research, corporate governance, technical operations or other disciplines related to the company's business.
 - (b) None of the relatives of an Independent director, for the purposes of sub-clauses (ii) and (iii) of clause (d) of section 149(6),—
 - (i) is indebted to the company, its holding, subsidiary or associate company or their promoters, or directors; or
 - (ii) has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, its holding, subsidiary

or associate company or their promoters, or directors of such holding company,

for an amount of fifty lakhs rupees, at any time during the two immediately preceding financial years or during the current financial year.

(c) **Declaration by Independent Director [Section 149(7)]:** Every independent director shall give a declaration that he meets the criteria of independence as provided in Section 149 (6) [refer Point No. (b) above] in the following manner:

- (1) at the **first meeting** of the Board in which he participates as a director; and
- (2) thereafter at the **first meeting of the Board in every financial year**; or
- (3) whenever there is **any change** in the circumstances which may affect his status as an independent director.

(d) **Code for independent directors [Section 149(8)]:** The company and independent directors shall abide by the provisions specified in Schedule IV to the Companies Act, 2013. As regards independent directors, Schedule IV specifies guidelines for professional conduct, role and functions, duties, manner of appointment and re-appointment, resignation and removal, provisions regarding separate meetings and evaluation mechanism.

(e) **Remuneration of Independent Directors [Section 149(9)]:** Notwithstanding anything contained in any other provision of this Act, but subject to the provisions of sections 197 and 198, an independent director **shall not be entitled to any stock option** and may receive remuneration by way of-

- (1) fee provided under Section 197(5),
- (2) reimbursement of expenses for participation in the Board and other meetings and
- (3) profit related commission as may be approved by the members.

Entitled to:	Not Entitled to:
Fee provided under section 197(5)	Any stock option
Reimbursement of expenses for participation in:	
(i) Board Meetings	
(ii) Other Meetings	
Profit related commission as may be approved by the members	

Note: According to Rule 4 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014, sitting fee required to be paid to an independent director shall not be less than the sitting fee which is payable to other directors of the company.

APPOINTMENT AND QUALIFICATIONS OF DIRECTORS

1.41

Provided that if a company has no profits or its profits are inadequate, an independent director may receive remuneration, exclusive of any fees payable under sub-section (5) of section 197, in accordance with the provisions of Schedule V.

(f) **Tenure [Section 149(10) & (11)]**: These provisions are stated as under:

- (i) (a) **Term**: Subject to the provisions of section 152 (Appointment of Directors), an independent director shall hold office for a term **up to 5 consecutive years** on the Board of a company.
- (b) **Eligibility for Re-appointment**: He shall be eligible for re-appointment on passing of a special resolution by the company and disclosure of such appointment in the Board's report.

Note: According to First Proviso to Section 169 (1), an independent director re-appointed for second term under Section 149(10) shall be removed by the company only by passing a **special resolution**.

- (ii) **Limit on holding of office**: An independent director shall not hold office for more than 2 consecutive terms.

Cooling period for appointment: However, he shall be eligible for appointment after the expiration of **3 years** of ceasing to be an independent director.

However, during the said period of 3 years he shall not be appointed in or be associated with the company in any other capacity, either directly or indirectly.

Note: It is clarified that for the purposes of sub-sections (10) and (11) of Section 149, any tenure of an independent director on the date of commencement of the Companies Act, 2013 shall not be counted as a term under those sub-sections.

Clarification issued by MCA

Appointment of 'Independent Directors' for less than 5 years [Refer Section 149(10) and (11)]: In terms of General Circular 14/2014, dated 09-06-2014, it is clarified by MCA that section 149(10) of the Act provides for a term of "upto five consecutive years" for an 'Independent Director'. As such while appointment of an 'Independent Director' for a term of less than five years would be permissible, appointment for any term (whether for five years or less) is to be treated as a one term under section 149(10) of the Act.

Further, under section 149(11) of the Act, no person can hold office of 'Independent Director' for more than 'two consecutive terms'. Such a person shall have to demit office after two consecutive terms even if the total number of years of his appointment in such two consecutive terms is less than 10 years. In such a case the person

completing 'consecutive terms of less than ten years' shall be eligible for appointment only after the expiry of the requisite cooling-off period of three years.

- (g) **Liability [Section 149(12)]:** As per section 149(12) of Act, following persons shall be liable for the following acts:

Parties Liable	For said Acts
(i) an independent director	- acts of omission or commission by a company which had occurred with his knowledge, - attributable through Board processes - with his consent or connivance, or - where he had not acted diligently
(ii) a non-executive director not being promoter or key managerial personnel	

- (h) **Retirement by rotation [Section 149(13)]:** The provisions of retirement of directors by rotation covered under sub-sections (6) and (7) of section 152 shall not be applicable to appointment of independent directors¹³.

- (i) **Independent Director is different from Nominee Director:** Appointment of a nominee director cannot be taken as a substitute for appointment of an independent director. Though a nominee director is also independent of the other Board members but this independence does not make him an independent director. He is appointed to safeguard the interest of the respective financial institution to which he belongs. His appointment triggers from the fact that his financial institution has given financial assistance to the company and he remains on the Board till the loan amount is repaid satisfactorily. Nominee director's appointment is mandatory only if the financial institution so desires because of the financial assistance given by it to the company; or any Government requires such appointment to represent its interest.

An independent director is appointed by the prescribed companies mandatorily. He is appointed to promote the confidence of the investing bodies, particularly minority shareholders. In fact, the companies in which his appointment is compulsory are much larger than other companies and therefore, they must always be well managed so that the confidence of the stakeholders is not shaken and their investment remains in safe hands. The appointment of independent director is a robust step in this direction. In the matter of good corporate governance, the regulators fall back upon him. The independent director at all times is required to maintain his independence and where circumstances arise which make him lose his independence, such fact must immediately be brought to the knowledge of the Board. The independent directors are required to hold at least one meeting in a financial year, without the attendance of non-independent directors and members of management.

¹³The provisions of retirement of directors by rotation covered under sub-sections (6) and (7) of Section 152 have been discussed later in the Chapter.

Exemptions

*In terms of Notification No.466(E) dated 5th June, 2015, as amended by Notification No. GSR 584 (E), dated 13-06-2017 a **Section 8 Company** is exempted from the provisions of sub-sections (4), (5), (6), (7), (8), (9), (10), (11), clause (i) of sub-section (12) and sub-section (13) of Section 149 of the Act, only if such company has not committed a default in filing its financial statements under Section 137 and Annual Return under Section 92 with the Registrar.*



13. MANNER OF SELECTION OF INDEPENDENT DIRECTORS AND MAINTENANCE OF DATA BANK OF INDEPENDENT DIRECTORS [SECTION 150]

Section 150 of the Act and Rule 6 of the Companies (Appointment and Qualifications of Directors) Rules, 2014, contain provisions regarding the manner of selection of independent directors and maintenance of databank of independent directors. These provisions are stated below:

- (i) **Maintenance of Data Bank of Independent Directors:** According to section 150(1), an independent director may be selected from a data bank containing names, addresses and qualifications of persons who are eligible and willing to act as independent directors, subject to the provisions contained in section 149(6).

Such data bank shall be maintained by any body, institute or association, as may be notified by the Central Government as having the expertise in creation and maintenance of such data bank and put on their website for the use by companies appointing such directors.

Rule 6 of the Companies (Appointment and Qualifications of Directors) Rules, 2014 lays down procedure required for a person who is eligible and willing to be appointed as an independent director. Accordingly-

- (1) Apply online for inclusion of name in the data bank: Every individual -
 - (a) who has been appointed as an independent director in a company, on the date of commencement of the Companies (Appointment and Qualifications of Directors) Fifth Amendment Rules, 2019, shall within a period of **thirteen months** from such commencement; or
 - (b) who intends to get appointed as an independent director in a company after such commencement, shall before such appointment, apply online to the institute for inclusion of his name in the data bank for a period of one year or five years or for his life-time, and from time to time take steps as specified in sub-rule (2), till he continues to hold the office of an independent director in any company:

Provided that any individual, including an individual not having DIN, may voluntarily apply to the institute for inclusion of his name in the data bank.

- (2) **Renewal of period for inclusion of his name in the data bank:** Every individual whose name has been so included in the data bank shall file an application for renewal for a further period of one year or five years or for his life-time, within a period of thirty days from the date of expiry of the period upto which the name of the individual was applied for inclusion in the data bank, failing which, the name of such individual shall stand removed from the data bank of the institute:

Provided that no application for renewal shall be filed by an individual who has paid life-time fees for inclusion of his name in the data bank.

- (3) **Submission of declaration of compliance to the Board:** Every independent director shall submit a declaration of compliance of sub-rule (1) and sub-rule (2) to the Board, each time he submits the declaration required under sub-section (7) of section 149 of the Act.
- (4) **To pass an online proficiency self assessment test:** Every individual whose name is so included in the data bank under sub-rule (1) shall pass an online proficiency self-assessment test conducted by the institute within a period two years from the date of inclusion of his name in the data bank, failing which, his name shall stand removed from the databank of the institute:

Exemptions from online proficiency self-assessment test: Provided that an individual shall not be required to pass the online proficiency self-assessment test when he has served for a total period of not less than three years as on the date of inclusion of his name in the data bank,-

- (A) **as a director or key managerial personnel**, as on the date of inclusion of his name in the databank, in one or more of the following, namely:-
- (a) listed public company; or
 - (b) unlisted public company having a paid-up share capital of rupees ten crore or more; or
 - (c) body corporate listed on any recognized stock exchange or in a country which is a member State of the Financial Action Task Force on Money Laundering and the regulator of the securities market in such member State is a member of the International Organization of Securities Commissions; or
 - (d) bodies corporate incorporated outside India having a paid-up share capital of US\$ 2 million or more; or

- (e) statutory corporations set up under an Act of Parliament or any State Legislature carrying on commercial activities; or
- (B) in the **pay scale of Director or equivalent or above** in any Ministry or Department, of the Central Government or any State Government, and having experience in handling,—
 - (i) the matters relating to commerce, corporate affairs, finance, industry or public enterprises; or
 - (ii) the affairs related to Government companies or statutory corporations set up under an Act of Parliament or any State Act and carrying on commercial activities.”
- (C) **in the pay scale of Chief General Manager or above** in the Securities and Exchange Board or the Reserve Bank of India or the Insurance Regulatory and Development Authority of India or the Pension Fund Regulatory and Development Authority and having experience in handling the matters relating to corporate laws or securities laws or economic laws :

Provided further that for the purpose of calculation of the period of three years referred to in the first proviso, any period during which an individual was acting as a director or as a key managerial personnel in two or more companies or bodies corporate or statutory corporations at the same time shall be counted only once.

“Provided also that the following individuals, who are or have been, for at least ten years :—

- (A) an advocate of a court; or
 - (B) in practice as a chartered accountant; or
 - (C) in practice as a cost accountant; or
 - (D) in practice as a company secretary, shall not be required to pass the online proficiency self-assessment test.”.
- (5) **Restoration of names in the databank:** Any individual whose name has been removed from the databank under sub-rule (4), may apply for restoration of his name on payment of fees of one thousand rupees and the institute shall allow such restoration subject to the following conditions, namely :-
- (i) his name shall be shown in a **separate restored category for a period of one year** from the date of restoration within which, he shall be required to pass the online proficiency self-assessment test and thereafter his name shall be included in the databank, only, if he passes the said online proficiency self-assessment test and in such case, the fees paid by him at the time of initial

registration shall continue to be valid for the period for which the same was initially paid; and

In case he **fails to pass the online proficiency self-assessment test within one year from the date of restoration**, his name shall be removed from the data bank and he shall be required to apply afresh under sub-rule (1) for inclusion of his name in the databank.

Explanation: For the purposes of this rule,-

- (a) the expression "institute" means the 'Indian Institute of Corporate Affairs at Manesar' notified under sub-section (1) of section 150 of the Companies Act, 2013 as the institute for the creation and maintenance of data bank of Independent Directors;
 - (b) an individual who has obtained a score of not less than fifty per cent., in aggregate in the online proficiency self-assessment test shall be deemed to have passed such test;
 - (c) there shall be no limit on the number of attempts an individual may take for passing the online proficiency self-assessment test.
- (ii) **Due diligence to be exercised by the company:** Further, the responsibility of exercising due diligence before selecting a person as an independent director from the data bank, shall lie with the company making such appointment [Proviso to Section 150(1)].
 - (iii) **Approval of Appointment in general meeting:** The appointment of independent director shall be approved by the company in general meeting as provided in section 152(2) and the explanatory statement annexed to the notice of the general meeting called to consider the said appointment shall indicate the justification for choosing the appointee for appointment as independent director. [Section 150(2)].
 - (iv) **Data bank to contain list of willing persons who desire to act as Independent Directors:** The data bank shall create and maintain data of persons willing to act as independent director in accordance with Rule 6 of the Companies (Appointment and Qualifications of Directors) Rules, 2014. [Section 150(3)]
 - (v) **Manner & procedure of selection specified by CG:** The Central Government may prescribe the manner and procedure of selection of independent directors who fulfill the qualifications and requirements specified under section 149 [Section 150(4)]

Exemption

*Notification No. 466(E) dated 5th June, 2015 as amended by Notification No. GSR 584 (E), dated 13-06-2017 has exempted a **Section 8 company** from the application of Section 150 of the Act, only if such company has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar.*



14. DUTIES OF DIRECTORS

Directors appointed in a company have various duties to perform. The foremost duty of the directors is to act honestly and diligently and in the best interest of the company so that the objective of wealth maximization is achieved for the stakeholders. In no case any business opportunity which falls within the ambit of the company be exploited by the directors for their own benefits.

A. Duties as per Section 166: Duties of directors, more particularly statutory duties, have been prescribed for the first time in the Statute. Section 166 specifies the following duties which are required to be accomplished by a director:

- (i) He shall **act in accordance with the articles** of the company, subject to the provisions of the the Companies Act, 2013.
- (ii) He shall **act in good faith** in order to promote the objects of the company for the benefit of its members as a whole. Further, he shall act in the best interests of the company, its employees, the shareholders, the community and for the protection of environment.
- (iii) He shall **exercise his duties with due and reasonable care**, skill and diligence and shall exercise independent judgment.
- (iv) He shall **not involve** in a situation in which he may have a **direct or indirect interest** that conflicts, or possibly may conflict, with the interest of the company.
- (v) He shall **not achieve any undue gain or advantage** either to himself or to his relatives, partners, or associates. In case such director is found guilty of making any undue gain, he shall be liable to pay an amount equal to that gain to the company.
- (vi) He shall **not assign his office** and if any assignment is so made, it shall be void.

The assignment of office has been made invalid because of the fact that the shareholders have elected a particular person as director for the management of their company. If such person assigns his office to some other person, the shareholders may not have faith in the other person; and therefore, a person who does not command the faith of the shareholders cannot be given the responsibility to manage the company. In other words, it is required of the original director to carry out his duties of directorship on his own without assigning them to some other person. Delegation of duties to other staff members, wherever permitted, is not akin to assignment of office.

Punishment for not accomplishing statutory duties: If any director of the company contravenes the provisions of Section 166, such director shall be punishable with fine which shall not be less than ₹ 1,00,000 but which may extend to ₹ 5,00,000.

B. Some Other Duties¹⁴: They are described as under:

- (i) **To file various documents:** It is the duty of the directors to file various documents required

¹⁴ This list of duties is not exhaustive.

- to be filed with the Registrar within the specified time limits. Similarly, wherever required, the requisite documents must also be filed with other statutory bodies.
- (ii) **To convene General Meetings:** As and when required, Annual General Meeting (AGM)¹⁵ and extraordinary general meetings (EGMs)¹⁶ need to be convened by the directors.
 - (iii) **To attend Board Meetings:** Board meetings is the platform where collective decisions are taken for managing the company profitably. It is statutorily required of a company to hold at least four board meetings every year¹⁷ and the gap between two board meetings must not exceed 120 days. However, a company may, as per the exigencies, hold more meetings than statutorily required and every director is duty-bound to attend them. A director, though, may not attend all the Board meetings held in a year but in case he remains absent from all such meetings held within a period of twelve months either with or without seeking leave of absence, he shall be deemed to have vacated his office¹⁸.
 - (iv) **To disclose interest¹⁹:** In the ordinary course, it is required of a director that his interest should not clash with the interests of the company *i.e.* he should not get himself benefitted from a transaction, the profit of which belongs to the company. If it happens and a director gets interested in a transaction belonging to the company, it is his duty to disclose such interest at the very first Board meeting he attends after becoming interested in the transaction. Thereafter, such interest should be disclosed in the first board meeting held in every financial year. In case there is any change in the disclosure already made by the director, such change needs to be brought in the knowledge of other directors in the first board meeting which he attends after occurring of such change. A detailed disclosure of interest and punishment for non-disclosure is discussed at the appropriate place.
 - (v) **To approve the annual financial statements²⁰:** Before seeking auditor's report, the annual financial statements *i.e.* balance sheet, statement of profit and loss, cash flow statement, etc. including consolidated financial statements, if any, are required to be approved by the directors.
 - (vi) **To approve and attach Board Report²¹:** A report by the Board of Directors containing requisite particulars on the affairs of the company including Directors' Responsibility Statement is required to be attached with the financial statements after its approval.
 - (vii) **To appoint first Auditors²²:** It is the duty of directors to appoint first auditors of the company.

¹⁵ Refer Section 96.

¹⁶ Refer Section 100.

¹⁷ Refer Section 173 (1). A company, if specifically exempted, may hold lesser number of Board Meetings in a year.

¹⁸ Refer Section 167 (1) (b).

¹⁹ Refer Section 184.

²⁰ Refer Section 134.

²¹ Refer Section 134.

²² Refer Section 139.



15. VACATION OF OFFICE OF DIRECTOR [SECTION 167]

Section 167 of the Act contains provisions detailing out as to when the office of a director shall become vacant. As soon as, any such event occurs, the director is required to demit the office of director of the company. These provisions are given as under:

(i) **Grounds for vacation:** According to Section 167 (1), the office of a director shall become vacant in case:

(a) he incurs any of the **disqualifications specified in section 164**;

However, if he incurs disqualification under section 164(2), the office of the director shall become vacant in all the companies, except the company which is in default under that sub-section;

(b) he **absents himself from all the meetings** of the Board of Directors held during a period of 12 months with or without seeking leave of absence of the Board;

(c) he **acts in contravention of the provisions of section 184** relating to entering into contracts or arrangements in which he is directly or indirectly interested;

(d) he **fails to disclose his interest** in any contract or arrangement in which he is directly or indirectly interested, in contravention of the provisions of section 184;

(e) he becomes **disqualified by an order** of a court or the Tribunal;

(f) he is **convicted by a court** of any offence, whether involving moral turpitude or otherwise and sentenced to imprisonment for 6 months or more.

Exception: The office shall not be vacated by the director in case of orders referred to in clauses (e) and (f)—

(i) for thirty days from the date of conviction or order of disqualification;

(ii) where an appeal or petition is preferred within thirty days as aforesaid against the conviction resulting in sentence or order, until expiry of seven days from the date on which such appeal or petition is disposed of; or

(iii) where any further appeal or petition is preferred against order or sentence within seven days, until such further appeal or petition is disposed of;

(g) he is **removed in pursuance of the provisions of the Companies Act, 2013** like when he is required to vacate office for disqualification incurred under Section 217 (6) (ii) i.e. conviction for committing an offence under Section 217;

(h) he, having been **appointed a director by virtue of his holding any office or other employment** in the holding, subsidiary or associate company, **ceases to hold such office or other employment** in that company.

Provision of additional ground for vacation by a private company: According to Section 167(4), a private company may provide any other ground for the vacation of the office of a director in addition to those specified above, through its articles.

- (ii) **Punishment:** Section 167(2) prescribes punishment in case of contravention of section 167(1). Thus, if a person functions as a director even when he knows that the office of director held by him has become vacant on account of any of the disqualifications specified in Section 167(1), he shall be punishable with fine of ₹ 1,00,000 extendable to ₹ 5,00,000.
- (iii) **All the Directors vacating the office:** Section 167(3) mentions about the eventuality when all the directors of a company vacate their offices under any of the disqualifications specified in Section 167(1). In that case, the promoter or, in his absence, the Central Government shall appoint the required number of directors who shall hold office till the directors are appointed by the company in the general meeting.



16. RESIGNATION OF DIRECTOR [SECTION 168]

Provisions regarding resignation of directors have been included in the Companies Act, 2013 for the first time. Section 168 read with Rule 15 and Rule 16 of the Companies (Appointment and Qualifications of Directors) Rules, 2014 deals with resignation of a director as under:

Notice of resignation in writing may be served to the company by the director

Board takes note on receipt of notice

Co. shall intimate Registrar within 30 days of receipt of notice in Form DIR-12

Fact of such resignation is given in the report of directors placed in the immediately following general meeting

Director forward copy of resignation with reasons to Registrar in 30 days from date of resignation in Form DIR-11 with fees.

Signing and Filing of Form DIR-11 in case of a Foreign Director: In case a company has already filed Form DIR-12 with the Registrar, a foreign director of such company resigning from his office may **authorise** in writing a practising chartered accountant or cost accountant in practice or

company secretary in practice or any other resident director of the company to sign Form DIR-11 and file the same on his behalf intimating the reasons for the resignation.

Clarification: MCA vide General Circular No. 3/15, dated 3rd March, 2015 has clarified that in the event of deactivation of Digital Signature Certificate (DSC) following *en masse* resignation of all the directors of a company before appointment of new directors in their places, where Form DIR-12 cannot be filed by a company due to lack of an authorized signatory director, the Registrars of Companies within their respective jurisdictions are authorized, on request from the stakeholders, and after due examination, to allow any one of the resigned director who was an authorized signatory director for the purpose of filing DIR-12 only along with additional fees, as applicable and subject to compliance of other provisions of Companies Act, 2013.

Effective date of resignation: The resignation of a director shall take effect:

(i) from the date on which the notice is received by the company,

OR

(ii) the date, if any, specified by the director in the notice,

whichever
is later

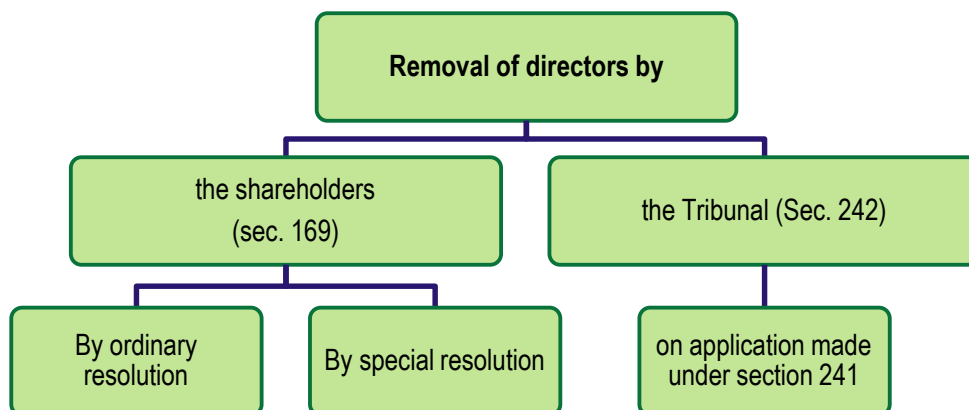
Liability: The director who has so resigned shall be liable even after his resignation for the offences which occurred during his tenure.

All the Directors tendering resignation: In case all the directors of a company resign from their offices, or vacate their offices under section 167, **the promoter** or, in his absence, **the Central Government** shall appoint the required number of directors who shall hold office till the directors are appointed by the company in general meeting.



17. REMOVAL OF DIRECTORS [SECTION 169]

A director of a company may be removed before completion of his term as director. Removal of directors is discussed here under the following heads:



I. Removal of Director by the Shareholders: Section 169 of the Act contains provisions for removal of directors by the shareholders. The way shareholders are empowered to appoint a director, in the same way they can also remove a director. The **procedure of removal** may be in the following manner:

(i) **Requirement of Ordinary Resolution²³:** A company may, by **ordinary resolution**, remove a director before the expiry of the period of his office **except the following**:

(a) when a director is appointed by the Tribunal under Section 242.

²⁴(b) when as per Section 163, two-thirds or more of the total number of directors are appointed according to the principle of proportional representation, then such directors cannot be removed.

For example, if a company has eight directors, of which six were appointed according to the principle of proportional representation. In such a case, only two directors which were not appointed following the system of proportional representation, can only be removed by the shareholders.

(ii) **Requirement of Special Resolution in case of removal of re-appointed independent director:** An independent director re-appointed for second term under Section 149(10) shall be removed by the company only by passing a **special resolution**.

Note: Under both the clauses (i) and (ii) above, the director to be removed shall be given a reasonable opportunity of being heard before his removal.

(iii) **Special Notice²⁵:** A special notice as per Section 115 shall be required for proposing any resolution to remove a director.

Special notice under Section 115 is required to be signed by:

(i) members holding not less than 1% of total voting power; or

(ii) members holding shares on which at least Rs. 5,00,000 has been paid in the aggregate.

Such notice shall be sent by the members not earlier than 3 months but at least 14 days before the meeting at which the resolution is desired to be moved.

(iv) **Action by the company²⁶:** On receipt of the special notice of a resolution to remove a director, the company shall forthwith send a copy thereof to the director concerned, and the director,

²³As per Section 169 (1).

²⁴As per Second Proviso to Section 169 (1).

²⁵As per Section 169 (2).

²⁶As per Section 169 (3).

whether or not he is a member of the company, shall be entitled to be heard on the resolution at the meeting.

- (v) **Representation by the director:** In case the director concerned makes a written representation to the company and requests that it should be notified to members, the company shall, if the time permits it to do so,-
- (a) **state the fact of the representation** having been made by the director in any notice of the resolution given to members of the company; and
 - (b) **send the representation to every member** of the company to whom notice of the meeting is sent (whether before or after receipt of the representation by the company).

In case, the representation is not sent as aforesaid due to insufficient time or for the company's default, the director may without prejudice to his right to be heard orally require that the representation shall be read out at the meeting.

Representation of director need not be sent²⁷: It is provided that representation need not be sent out and read out at the meeting if, on the application either of the company or of any other aggrieved person, the Tribunal is satisfied that the rights of representation are being abused to secure needless publicity for defamatory matter.

Further, the Tribunal may order the director concerned (notwithstanding that he is not a party to it) to make payment in whole or in part of the costs incurred by the company on the application so made to the Tribunal.

- (vi) **Filling of vacancy²⁸:** The vacancy resulting from the aforesaid removal if he had been appointed by the company in general meeting or by the Board, may be filled in by the appointment of another director at the same meeting at which the director is removed, provided special notice of the proposed appointment has been given.

Non-Filling of vacancy²⁹: If the vacancy is not filled in the same meeting as above, then it may be filled as a casual vacancy provided that the director who was so removed from office shall not be reappointed as a director.

- (vii) **Period of holding of office by new director³⁰:** A director so appointed shall hold office for the remaining period for which the director who has been removed would have held office if he had not been removed.

²⁷As per Proviso to Section 169 (4).

²⁸As per Section 169 (5).

²⁹As per Section 169 (5).

³⁰As per Section 169 (7).

- (viii) **Payment of compensation**³¹: A person so removed as director shall not be deprived of his rights to compensation or damages payable to him in respect of the premature termination of the directorship, or terms of his appointment as director or of any appointment terminating with that as a director. The restrictions imposed by Section 202 are also to be kept under consideration while making payment of compensation for loss of office of directorship.
- (ix) **No restriction imposed by Section 169**³²: Nothing in Section 169 shall be taken as derogating from any power to remove a director under any other provisions of the Companies Act, 2013.

In other words, Section 169 does not impose any restriction on any other power available under some other provisions of the Companies Act, 2013 which allows removal of a director.

II. **Removal of Director by the Tribunal**: According to Section 242, a director may be removed by the Tribunal where an application has been made to it under Section 241 for prevention of oppression and mismanagement in the company. The Tribunal is also empowered to terminate, set aside or modify any agreement between the company and any of its directors on such terms and conditions which in the opinion of Tribunal are just and equitable.

According to Section 243, a director so removed as per the order of Tribunal shall not be entitled to claim any compensation for loss of his office. Further, he shall not be offered appointment as director for a period of **five years** from the date of the order without first seeking the leave of the Tribunal.

18. REGISTER OF DIRECTORS AND KEY MANAGERIAL PERSONNEL AND THEIR SHAREHOLDING [SECTION 170]

A company is required to maintain a register of directors and key managerial personnel and their shareholding under Section 170 of the Act. These provisions are as under:

Every company shall keep at its registered office a register containing the prescribed particulars of its directors and key managerial personnel. The prescribed particulars shall include details of securities held by each of them in the company or its holding, subsidiary, subsidiary of its holding companies or associate companies. In this respect Rule 17 of the Companies (Appointment and Qualifications of Directors) Rules, 2014, is relevant. It prescribes the following **particulars to be included in the Register**:

- (a) Director Identification Number (optional for key managerial personnel);

³¹As per Section 169 (8) (a).

³²As per Section 169 (8) (b).

- (b) present name and surname in full;
- (c) any former name or surname in full;
- (d) father's name, mother's name and spouse's name(if married) and surnames in full;
- (e) date of birth;
- (f) residential address (present as well as permanent);
- (g) nationality (including the nationality of origin, if different);
- (h) occupation;
- (i) date of the board resolution in which the appointment was made;
- (j) date of appointment and reappointment in the company;
- (k) date of cessation of office and reasons therefor;
- (l) office of director or key managerial personnel held or relinquished in any other body corporate;
- (m) membership number of the Institute of Company Secretaries of India in case of Company Secretary, if applicable; and
- (n) Permanent Account Number (mandatory for key managerial personnel if not having DIN);

In addition to the above details, the company shall also include in the Register the **details of securities held by them** in the company, its holding company, subsidiaries, subsidiaries of the company's holding company and associate companies relating to:

- (a) the number, description and nominal value of securities;
- (b) the date of acquisition and the price or other consideration paid;
- (c) date of disposal and price and other consideration received;
- (d) cumulative balance and number of securities held after each transaction;
- (e) mode of acquisition of securities ;
- (f) mode of holding – physical or in dematerialized form; and
- (g) whether securities have been pledged or any encumbrance has been created on the securities.

Filing of Return in Form DIR-12 with the Registrar:Section 170(2) read with Rule 18 of the Companies (Appointment and Qualifications of Directors) Rules, 2014 requires a company to file a return in Form DIR-12 in respect of its directors and the key managerial personnel after paying the prescribed fee as under:

- (a) within 30 days from the appointment; and
- (b) within 30 days of any change taking place.

Exemption

*Section 170 of the Companies Act, 2013 shall not apply to a **Government company** in which the entire share capital is held by the Central Government, or by any State Government or Governments or by the Central Government or by one or more State Government subject to the condition that such Government company has not committed a default in filing its financial statements under Section 137 or Annual return under Section 92 with the registrar. [Notification No.G.S.R. 463(E), dated 5th June, 2015 as amended by Notification No. GSR 582 (E), dated 13-06-2017].*

**19. MEMBERS' RIGHT TO INSPECT [SECTION 171]**

The members of the company have a right to inspect the register of directors and key managerial personnel under Section 171 of the Act. Accordingly:

- (i) **Timing for inspection:** The register of directors and key managerial personnel shall be kept open for inspection during **business hours**. The members shall have the right to take extracts therefrom and copies thereof on request and the same will be provided to them within 30 days free of cost. [Refer Section 171(1)(a)]
- (ii) **Open for inspection:** The register shall also be kept open for inspection at every annual general meeting of the company and shall be made accessible to any person attending the meeting. [Refer Section 171(1)(b)]
- (iii) **Registrar to order in case of refusal:** If any inspection during business hours is refused, or if any copy required as above is not sent within thirty days from the date of receipt of such request, the registrar shall on an application made to him order immediate inspection and supply of copies. [Refer Section 171(2)]

Exemptions

*Section 171 shall not apply to a **Government company** in which the entire share capital is held by the Central Government, or by any State Government or Governments or by the Central Government or by one or more State Government subject to the condition that such Government company has not committed a default in filing its financial statements under Section 137 or Annual return under Section 92 with the registrar. [Notification No.G.S.R. 463(E), dated 5th June, 2015 as amended by Notification No. GSR 582 (E), dated 13-06-2017].*



20. PUNISHMENT [SECTION 172]

Section 172 of the Act provides that if a company contravenes any of the provisions of Chapter XI containing Sections 149 to 171 and for which no specific penalty or punishment is provided therein, the company and every officer of the company who is in default shall be liable to a penalty of fifty thousand rupees, and in case of continuing failure, with a further penalty of five hundred rupees for each day during which such failure continues, subject to a maximum of three lakh rupees in case of a company and one lakh rupees in case of an officer who is in default.

In the decided case of *Jalpower Corporation Ltd. v. Registrar of Companies*, it was held that where there was delay in appointing woman director and application was filed for compounding of offence, same was to be permitted for company and all its directors, though application for compounding was filed by company and two of its directors on payment of penalty by each of directors.

This was decided in as per Section 149, read with section 172 and section 441, of the Companies Act, 2013 and rule 3 of the Companies (Appointment and Qualification of Directors) Rules, 2014. In the given case, Applicant company appointed woman director after a delay of 180 days. ROC filed complaint before EO. As belated appointment did not cause any prejudice to any creditors of company or public at large, therefore, application was filed by company and two of its directors for compounding of offence.

Here it was held that since offence was committed by company and all its 4 directors, so composition of offence was to be permitted for company and all 4 directors, though application for compounding was filed by company and two of its directors. All directors here had to pay fine and ROC should bring issue of compounding of offence to notice of Special Judge for Economic Offence.

TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. Mr. Q, a Director of PQR Limited, is proceeding on a foreign tour covering entire Europe for four months. He proposes to appoint Mr. Y as an alternate Director to act on his behalf during his absence. The Articles of Association of PQR Limited provide for the appointment of alternate Directors. Mr. Q claims that he has a right to appoint alternate Director of his choice. Which of the following options is applicable in the given situation:
 - (a) Claim made by Mr. Q to appoint Mr. Y as alternate Director is valid as the Articles of Association of PQR Limited provide for such appointment.
 - (b) Claim made by Mr. Q to appoint Mr. Y as alternate Director is not valid as the authority to appoint alternate Director has been vested in the Board of Directors only and that too subject to empowerment by the Articles of Association.
 - (c) Mr. Y cannot be appointed as an alternate Director in place of Mr. Q since Mr. Q is proceeding on a foreign tour covering entire Europe for four months only which is less than the required absence of minimum six months.
 - (d) Mr. Y cannot be appointed as an alternate Director in place of Mr. Q since Mr. Q is proceeding on a foreign tour covering entire Europe for four months which is more than the required absence of maximum three months.

2. In compliance with the Companies Act, 2013, at least one woman director shall be on the Board of the prescribed class or classes of companies. Ms. Riya is keen to seek the office of woman director in a company. Which of the following companies is mandatorily required to appoint a woman director where Ms. Riya can hold such office:
 - (a) PQR Limited, an unlisted company, whose paid-up share capital is not exceeding 150 crore rupees as per the last date of latest audited financial statements is mandatorily required to appoint a woman director.
 - (b) ABC Limited, a listed company, whose turnover is 250 crore rupees as per the last date of latest audited financial statements is mandatorily required to appoint a woman director.
 - (c) XYZ Limited, an unlisted company, whose turnover is not more than 300 crore rupees as per the last date of latest audited financial statements is mandatorily required to appoint a woman director.
 - (d) BCZ Limited, an unlisted company whose paid-up share capital is not exceeding 100 crore and turnover is less than 300 crore rupees as per the last date of latest audited financial statements is mandatorily required to appoint a woman director.

3. *Kutumb Agro Limited (KAL), a newly incorporated company, has not mentioned the names of the first Directors in its Articles of Association. There are eight subscribers to the Memorandum of Association including Parivaar Agro Private Limited. From the following four options, choose the one which indicates as to who shall be deemed to be the first Directors of KAL when nothing is mentioned in the Articles?*
- (a) *All the eight subscribers to the Memorandum of Association of KAL shall be deemed to be the first Directors.*
 - (b) *Except Parivaar Agro Private Limited, all other subscribers to the Memorandum of Association of KAL shall be deemed to be the first Directors.*
 - (c) *The shareholders shall appoint the first Directors in the General Meeting of KAL.*
 - (d) *Out of the eight subscribers to the Memorandum of Association, the first Directors being three individuals shall be nominated by Srinivas, the Chartered accountant who has signed the Memorandum as witness and they shall be deemed to be the first Directors of KAL.*
4. *The turnover of XYZ Components Limited as on the last date of latest audited financial statements is 400 crore rupees. An intermittent vacancy of a woman Director arose on June 15, 2021 due to the resignation of Ms. Swati. The immediate Board Meeting after the resignation of Ms. Swati was held on October 10, 2021. From the following options, choose the one which indicates the date by which the vacancy of the woman Director must be filled by XYZ Components Limited.*
- (a) *July 14, 2021*
 - (b) *August 14, 2021*
 - (c) *September 14, 2021*
 - (d) *October 10, 2021*
5. *Mr. Nagarjuna, one of the directors of MGT Mechanics Limited, due to his own business interests, decided to resign as director and accordingly, sent his resignation letter dated 12th June, 2021 to the company stating that he intends to resign w.e.f. 15th June, 2021. Since no communication in relation to his resignation was received from MGT Mechanics Limited, he sent an e-mail on 17th June, 2021 enquiring about the receipt of his resignation letter by the company but there was no response. However, MGT Mechanics Limited received his resignation letter on 18th June, 2021. Out of the following four options, choose the one which indicates the correct date from which his resignation will be effective:*
- (a) *12th June, 2021*
 - (b) *15th June, 2021*
 - (c) *17th June, 2021*
 - (d) *18th June, 2021*

6. Mr. Z is proposed to be appointed as the Director in RLP Mechanics Limited. It is noteworthy that Mr. Z already holds directorship in one dormant company, two Section 8 companies, eight public limited companies and nine private limited companies. However, out of nine private limited companies, two are subsidiaries of public limited companies. In the given circumstances, is it possible for Mr. Z to accept another directorship in RLP Mechanics Limited without attracting any invalidity:
- It is not possible for Mr. Z to accept another directorship in RLP Mechanics Limited since he is already holding directorships in twenty companies.
 - It is not possible for Mr. Z to accept another directorship in RLP Mechanics Limited since he is already holding directorships in eight public limited companies and two such private limited companies which are subsidiaries of public limited companies.
 - It is possible for Mr. Z to accept another directorship in RLP Mechanics Limited since Section 8 companies and dormant companies are excluded while calculating the limit of twenty companies.
 - It is possible for Mr. Z to accept another directorship in RLP Mechanics Limited since there is no limit on holding any number of directorships.

Descriptive Questions

- The Articles of Association of Rajasthan Toys Private Limited provide that the maximum number of Directors in the company shall not exceed 10. Presently, the company has 8 directors. Its Board of Directors desires to increase the number of directors from 8 to 16. Advise whether under the provisions of the Companies Act, 2013, the Board can do so?
- ADJ Limited has 10 directors on its Board. Two of the directors have retired by rotation at an Annual General Meeting. The place of retiring directors is not so filled up and the meeting has also not expressly resolved 'not to fill the vacancy'. Since the AGM could not complete its business, it is adjourned till the same day in the next week, at the same time and place. At this adjourned meeting also the place of retiring directors could not be filled up, and the meeting has also not expressly resolved 'not to fill the vacancy'.

Referring to the provisions of the Companies Act, 2013, decide:

- Whether in such a situation the retiring directors shall be deemed to have been re-appointed at the adjourned meeting?
- What will be your answer in case at the adjourned meeting, the resolutions for re-appointment of these directors were lost?
- Whether such directors can continue in case the directors do not call the Annual General Meeting?

3. *Prince Ltd. desires to appoint an additional director on its Board of directors. The Articles of the company confer upon the Board to exercise the power to appoint such a director. As such M is appointed as an additional director. In the light of the provisions of the Companies Act, 2013, examine*
 - (i) Whether M can continue as director if the annual general meeting of the company is not held within the stipulated period and is adjourned to a later date?
 - (ii) Can the power of appointing additional director be exercised at the Annual General Meeting by the members?
 - (iii) As the Company Secretary of the company what checks would you make after M is appointed as an additional director?
4. *The Board of Directors of XYZ Ltd. filled up a casual vacancy caused by the death of Mr. P by appointing Mr. C as a director on 3rd April, 2019 which was subsequently approved by the members in the immediate next general meeting. Unfortunately Mr. C expired on 15th May, 2019 after working about 40 days as a director. The Board now wishes to fill up the casual vacancy by appointing Mrs. C in the forthcoming meeting of the Board. Advise the Board in this regard keeping in view the provisions of the Companies Act, 2013.*
5. *Mr. John is a director of MNC Ltd., which had accepted deposits from public. The financial position of MNC Ltd. took a southward turn and became bad to worse and ultimately, it failed to repay the deposits which fell due for payment on 10th April, 2018 and such repayment has not been made till 5th May, 2019. Another company JKL Ltd. wants to appoint the said Mr. John as its director at its annual general meeting to be held on 6th May, 2019. You are required to state with reference to the provisions of the Companies Act, 2013 whether Mr. John can be appointed as a director of JKL Ltd.*
6. *XYZ Limited is an unlisted public company having a paid-up share capital of twenty crore rupees as on 31st March, 2019 and a turnover of one hundred fifty crore rupees during the year ended 31st March, 2019. The total number of directors is thirteen.*

Referring to the provisions of the Companies Act, 2013 answer the following:

- (i) State the minimum number of independent directors that the company should appoint.
 - (ii) How many independent directors are to be appointed in case XYZ Limited is a listed company?
7. *Bright Motors (P) Limited at the Annual General Meeting (AGM) held on 30.09.2016 appointed Mr. Anmol as a Non-Executive Director on the Board of the company for a period of three years. On 2nd October, 2017, Mr. Anmol suffered a severe heart failure and expired. The Board of Directors of the company on 16th October, 2017 appointed Mr. Prateek to fill the casual vacancy so created. The appointment of Mr. Prateek was made for a term of three years by the Board. Subsequently at the AGM held on 29-09-2018, Mr. Prateek's appointment was not proposed or approved as the Board was of the view that it is not required. But the CFO*

of the company is of the opinion that the Board of Directors have contravened the provisions of the Companies Act, 2013 in respect of non-approval of the appointment of Mr. Prateek and his office tenure. Decide.

8. Mr. Dhruv is a Director of LT Limited and XT Limited respectively. LT Limited did not file its financial statements for the year ended 31st March, 2016, 2017 & 2018 respectively with the Registrar of Companies (ROC) as mandated under the Companies Act, 2013. LT Limited also did not pay interest on loans taken from a Public Financial Institution from 1st April, 2017 and also failed to repay matured deposits taken from public on due dates from 1st April, 2017 onwards.

Answer the legality of the following in the light of the relevant provision of the Companies Act, 2013:

- (i) Whether Mr. Dhruv is disqualified under Companies Act, 2013 and if so, whether he can continue as a Director in LT Limited? Further can he also seek reappointment when he retires by rotation at the AGM of XT Limited scheduled to be held in September, 2019?
 - (ii) Mr. Dhruv is proposed to be appointed as an Additional Director of MN Limited in June 2019. Is he eligible to be appointed as an Additional Director in MN Limited? Decide.
9. You are the CFO and in-charge of legal compliances of large multi-national company in India. The Board of Directors of the Company comprises of directors who are Indian as well as Foreign Nationals. Mr. "X", who is a Director (Business Development) on the Board is very often on business tour abroad. He approached you and wants to know from you the regulatory provisions of the Companies Act, 2013 relating to appointment of Alternate Directors. Analyse the following situations and advise suitably. Mr. X referring to the provisions of the Companies Act, 2013.
 - (a) To how many directors can a person be appointed as an alternate director and how many votes does he have in one Board Meeting.
 - (b) In case of private company, where an alternate director is appointed in place of a non-executive director whose term is indefinite, then, what will be the tenure of such alternate director, provide the original director does not return to India for a longer period say 3-4 years?
 - (c) Can an Executive Director/Whole Time Director/Managing Director appoint alternate directors?
10. Mr. 'R' holds directorship in 10 Public Companies and 11 Private Companies as on 31.05.2019. One of the above Private Company is a dormant Company. Apart from the dormant Company, on 30.06.2019 a Private Company (in which Mr. R is holding directorship) has become a subsidiary of a Public Company.

In the light of the provisions of the Companies Act, 2013 examine and decide:

- (i) *The validity of holding directorship of Mr.'R' with reference to number of directorship as on 31.05.2019 and as on 30.06.2019.*
- (ii) *Whether a Company has power to specify any lesser number of Companies in which a director of the Company may act as a director?*

ANSWERS

Answer to Multiple Choice Questions

1.	b	2.	b	3.	b	4.	d	5.	d
6.	b								

Answer to Descriptive Questions

1. Under Section 149(1) of the Companies Act, 2013 every company shall have a Board of Directors consisting of individuals as directors and shall have a minimum number of 3 directors in the case of a public company, 2 directors in the case of a private company, and one director in the case of a One Person Company. The maximum number of directors shall be 15.

The First Proviso to Section 149(1) states that a company may appoint more than 15 directors after passing a special resolution.

From the provisions of section 149 (1) as above, though the minimum number of directors may vary depending on whether the company is a public, private or a one person company, the maximum number of directors is same for all types of companies i.e. 15 directors.

In the given case since the number of directors is proposed to be increased from 8 to 16, the company will be required to comply with the following provisions:

- (i) Alter its Articles of Association as per the provisions of Section 14 of the Act by passing a special resolution, so as to increase the number of directors in the Articles from 10 to 16;
- (ii) Also take approval for increasing the maximum number of directors from 8 to 16 by means of a special resolution passed by the members at a duly convened general meeting.

2. Retiring director – When to be deemed director?

In accordance with the provision of the Companies Act, 2013, as contained in section 152(7)(a) which provides that if at the annual general meeting at which a director retires and the vacancy is not so filled up and the meeting has not expressly resolved not to fill the vacancy, the meeting shall stand adjourned to same day in the next week, at the same time

and place, or if that day is a national holiday, till the next succeeding day which is not a holiday, at the same time and place.

Section 152(7)(b) further provides that if at the adjourned meeting also, the place of the retiring director is not filled up and that meeting also has not expressly resolved not to fill the vacancy, the retiring director shall be deemed to have been re-appointed at the adjourned meeting, unless at the adjourned meeting or at the previous meeting a resolution for the re-appointment of such director was put and lost or he has given a notice in writing addressed to the company or the Board of Directors expressing his desire not to be re-elected or he is disqualified.

Therefore, in the given circumstances answers to the asked questions shall be as under:

- (i) In the first case, applying the above provisions, the retiring directors shall be deemed to have been re-appointed.
 - (ii) In the second case, where the resolutions for the reappointment of the retiring directors were lost, the retiring directors shall not be deemed to have been re-appointed.
 - (iii) Section 152(6)(c) states that $\frac{1}{3}^{\text{rd}}$ of the rotational directors shall retire at every AGM. Accordingly, the directors will retire as soon as the AGM is held on its due date. Further, as per Section 96 (dealing with Annual General Meeting), every company other than a One Person Company is required to hold an Annual General Meeting in each year. Hence, it is necessary for the company to hold the AGM, where the directors liable to retire by rotation shall retire. In case AGM is not held till the last date on which it should have been held, the term of retiring directors ends on this last date and it can not be extended till the new date when the AGM shall be held. As the calling of the AGM is the duty and responsibility of the directors, they by omitting to call the AGM on its due date cannot take advantage of their own fault and by that means cannot extend their own continuance in the office for any period of their choice and as long as the holding of the next AGM does not take place.
3. Section 161(1) of the Companies Act, 2013 provides that the articles of association of a company may confer on its Board of Directors the power to appoint any person, other than a person who fails to get appointed as a director at the general meeting, as an additional director at any time and such director will hold office upto the date of the next annual general meeting or the last date on which such annual general meeting should have been held, whichever is earlier.
- (i) M cannot continue as director till the adjourned annual general meeting, since he can hold the office of directorship only up to the date of the next annual general meeting or the last date on which the annual general meeting should have been held, whichever is earlier. Such an additional director shall vacate his office latest on the date on which the annual general meeting should have been held under Section 96 of the Companies

Act, 2013. He cannot continue in the office on the ground that the meeting was not held or it could not be called within the time prescribed.

- (ii) The power to appoint additional directors vests with the Board of Directors and not with the members of the company. The only condition is that the Board must be conferred such power by the articles of the company.
- (iii) As a Company Secretary, I would put the following checks in place in respect of M's appointment as an additional director:
 - (a) He must have got the Directors Identification Number (DIN).
 - (b) He must furnish the DIN and a declaration that he is not disqualified to become a director under the Companies Act, 2013.
 - (c) He must give his written consent in Form DIR-2 on or before his appointment as director and such consent stands filed with the Registrar within 30 days of his appointment.
 - (d) His appointment is made by the Board of Directors.
 - (e) His name is entered in the statutory records as required under the Companies Act, 2013.

4. Section 161(4) of the Companies Act, 2013 provides that if the office of any director appointed by the company in general meeting is vacated before his term of office expires in the normal course, the resulting casual vacancy may, in default of and subject to any regulations in the articles of the company, be filled by the Board of Directors at a meeting of the Board which shall be subsequently approved by members in the immediate next general meeting.

Further, any person so appointed shall hold office only up to the date up to which the director in whose place he is appointed would have held office if it had not been vacated.

In view of the above provisions, in the given case, the appointment of Mr. C in place of the deceased director Mr. P was in order. In normal course, Mr. C could have held his office as director up to the date to which Mr. P would have held the same.

However, Mr. C expired on 15th May, 2018 and again a vacancy has arisen in the office of director owing to death of Mr. C who was appointed by the board and approved by members to fill up the casual vacancy resulting from P's demise. Vacancy arising on the Board due to vacation of office by the director appointed to fill a casual vacancy in the first place, does not create another casual vacancy as section 161 (4) clearly mentions that such vacancy is created by the vacation of office by any director appointed by the company in general meeting. Hence, the Board cannot fill the vacancy arising from the death of Mr. C who was appointed to fill a casual vacancy.

The Board may however appoint Mrs. C as an additional director under section 161 (1) of the Companies Act, 2013 provided the articles of association authorise the Board to do so, in

which case Mrs. C will hold the office up to the date of the next annual general meeting or the last date on which the annual general meeting should have been held, whichever is earlier.

5. Section 164 (2) (b) of the Companies Act, 2013 states that where a person is or has been a director of a company which has failed to repay its deposit on due date and such failure continues for one year or more, then such person shall not be eligible to be appointed as a director of any other company for a period of five years from the date on which such company, in which he is a director, failed to repay its deposits.

In the instant case, MNC Ltd., has failed to repay its deposit on due dates and the default continues for more than one year. Hence, Mr. John will not be eligible to be appointed as a director of JKL Ltd.

6. (i) According to Rule 4(1) of the Companies (Appointment and Qualifications of Directors) Rules, 2014, the following class or classes of companies shall have at least 2 directors as independent directors:
- (1) the Public Companies having paid up share capital of 10 crore rupees or more; or
 - (2) the Public Companies having turnover of 100 crore rupees or more; or
 - (3) the Public Companies which have, in aggregate, outstanding loans, debentures and deposits, exceeding 50 crore rupees.

In the present case, XYZ Limited is an unlisted public company having a paid-up capital of ₹ 20 crore as on 31st March, 2019 and a turnover of ₹ 150 crore during the year ended 31st March, 2019. Accordingly, as per stated Rules it must have at least 2 directors as independent directors.

- (ii) According to Section 149(4) of the Companies Act, 2013, every listed public company shall have at least one-third of the total number of directors as independent directors. The Explanation to Section 149(4) specifies that any fraction contained in such one-third numbers shall be rounded off as one.

In the present case, XYZ Limited is a listed company and the total number of directors is 13. Hence, in this case, XYZ Limited must have atleast 5 directors ($1/3$ of 13 is 4.33 rounded as 5) as independent directors.

Explanation to Rule 4 of the Companies (Appointment and Qualifications of Directors) Rules, 2014 clarifies that for the purpose of this Rule the paid up share capital or turnover or outstanding loans, debentures and deposits, as the case may be, as existing on the last date of latest audited financial statements shall be taken into account.

In the present case, it is mentioned that paid up capital of XYZ Limited is ₹20 crore as on 31st March, 2019 and turnover is ₹150 crore during the year ended 31st March, 2019. It is, therefore, assumed that 31st March, 2019 is the last date of latest audited financial statements.

7. According to section 161(4) of the Companies Act, 2013, if the office of any director appointed by the company in general meeting is vacated before his term of office expires in the normal course, the resulting casual vacancy may, in default of and subject to any regulations in the articles of the company, be filled by the Board of Directors at a meeting of the Board which shall be subsequently approved by members in the immediate next general meeting.

Provided that any person so appointed shall hold office only up to the date up to which the director in whose place he is appointed would have held office if it had not been vacated.

In the given question, the casual vacancy caused due to death of Mr. Anmol (who was appointed by the company in AGM held on 30.9.2016, for a period of 3 years) is filled by the Board of Directors by appointing Mr. Prateek for a period of three years. However, the appointment of Mr. Prateek for a period of three years is in contravention of above stated provisions as he can hold office only up to the date up to which Mr. Anmol would have held office if it had not been vacated.

Further, as per the provisions of the Act, the appointment of Mr. Prateek ought to be approved by members in the immediate next general meeting. However, the appointment of Mr. Prateek was not even proposed or approved in the AGM held on 29.9.2018. Hence, the appointment of Mr. Prateek is in contravention of the provisions of the Companies Act, 2013. Therefore, the opinion of CFO is correct.

8. According to section 164(2) of the Companies Act, 2013, no person who is or has been a director of a company which has not filed financial statements or annual returns for any continuous period of three financial years; or has failed to repay the deposits accepted by it or pay interest thereon or to redeem any debentures on the due date or pay interest due thereon or pay any dividend declared and such failure to pay or redeem continues for one year or more, shall be eligible to be re-appointed as a director of that company or appointed in other company for a period of five years from the date on which the said company fails to do so.

Provided that where a person is appointed as a director of a company which is in default of clause (a) or clause(b), he shall not incur the disqualification for a period of six months from the date of his appointment.

Also, according to section 167(1)(a), the office of a director shall become vacant in case he incurs any of the disqualifications specified in section 164;

Provided that where he incurs disqualification under sub-section (2) of section 164, the office of the director shall become vacant in all the companies, other than the company which is in default under that sub-section.

Thus, in the light of the said provisions of the Act and the facts of the question:

- (i) Yes, Mr. Dhruv is disqualified under the Companies Act, 2013, as LT Limited did not file financial statements for a period of three years. Also, the LT Limited has defaulted in the repayment of matured deposits taken from public since 1st April, 2017 (i.e. the default has continued for more than one year).

Mr. Dhruv can continue as a director in LT Limited as proviso to section 167(1)(a) provides that where the director incurs disqualification under section 164(2), the office of the director shall become vacant in all the companies, other than the company which is in default. Whereas he has to vacate the office of director in XT Limited.

Mr. Dhruv cannot be reappointed (in the AGM to be held in September 2019) as director in XT Limited.

- (ii) Mr. Dhruv cannot be appointed as an Additional Director (in the AGM to be held in June 2019) of MN Limited because as per section 164(2), he is not eligible to be appointed in other company for a period of five years from the date of such default.

9. (a) According to Section 161(2) of the Companies Act, 2013, the Board of Directors of a company may, if so authorized by its articles or by a resolution passed by the company in general meeting, appoint a person, not being a person holding any alternate directorship for any other director in the company or holding directorship in the same company, to act as an alternate director for a director during his absence for a period of not less than three months from India.

According to section 165, no person shall hold office as a director, including any alternate directorship, in more than twenty companies at the same time. However, the maximum number of public companies in which a person can be appointed as a director shall not exceed ten.

Hence, in the instant case, a person can be appointed as an alternate director for only one director in the **same company** but maximum twenty different companies.

An alternate director will have only one vote as he can hold alternate directorship for one director only in the same company.

- (b) According to second proviso to section 161(2), an alternate director shall not hold office for a period longer than that permissible to the director in whose place he has been appointed and shall vacate the office if and when the director in whose place he has been appointed returns to India.

Third proviso says that if the term of office of the original director is determined before he so returns to India, any provision for the automatic re-appointment of retiring directors in default of another appointment shall apply to the original, and not to the alternate director.

Hence, in the instant case, the alternate director shall hold office till the time original director returns to India, even if the period is as long as 3-4 years.

- (c) As per section 161(2), the Board of Directors of a company may, if so authorized by its articles or by a resolution passed by the company in general meeting, appoint a person, not being a person holding any alternate directorship for any other director in the company or holding directorship in the same company, to act as an alternate director for a director during his absence for a period of not less than three months from India.

From the above provision, it is clear that an alternate director can be appointed for any director. Hence, an alternate director can be appointed for Executive director/ Whole Time Directors / Managing Director however, not by them but by the Board of Directors.

10. (i) According to Section 165 of the Companies Act, 2013, no person shall hold office as a director, including any alternate directorship, in more than twenty companies at the same time. Whereas that the maximum number of public companies in which a person can be appointed as a director shall not exceed ten.

For reckoning the limit of public companies in which a person can be appointed as director, directorship in private companies that are either holding or subsidiary company of a public company shall be included.

For reckoning the limit of directorships of twenty companies, the directorship in a dormant company shall not be included.

In the instant case, holding of directorship of Mr. R as on 31.05.2019 is valid as he is holding directorship in 10 public companies and in 11 private companies out of which one company is dormant company. So, maximum directorship he is holding in 20 companies.

Holding of directorship of Mr. R as on 30.06.2019 is not valid, as on 30.06.2019 a private company (in which Mr. R is holding directorship) has become a subsidiary of a public company. Accordingly, it means that this private company shall be deemed to be included in the limit of public companies and thereby increasing the number of public companies in which he is holding directorship to 11 and making it invalid.

- (ii) According to section 165(2), Subject to the provisions of sub-section (1), the members of a company may, by special resolution, specify any lesser number of companies in which a director of the company may act as directors.

[illegible]

CHAPTER

2

APPOINTMENT AND REMUNERATION OF MANAGERIAL PERSONNEL



LEARNING OUTCOMES

After studying this chapter, the students would be able to:

- ❑ Describe the provisions relating to appointment of Managing Director, Whole Time Director and Manager.
- ❑ Explain the provisions regarding appointment of Key Managerial Personnel (KMPs).
- ❑ Comprehend the concept of maximum managerial remuneration and managerial remuneration payable in case of absence or inadequacy of profits.
- ❑ Compute and calculate profits for the purpose of managerial remuneration and recovery of managerial remuneration in certain cases.
- ❑ Explain the concepts of compensation for loss of office of Managing or Whole Time Director or Manager.
- ❑ Explain about the functions of Company Secretary and requirements for Secretarial Audit.



1. INTRODUCTION

This Chapter deals with the appointment of managerial personnel and managerial remuneration payable to them as per the applicable provisions of the Companies Act, 2013, with relevant Rules made thereunder and Schedule V.

MEANING OF CERTAIN TERMS

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

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

"Company Secretary" or "secretary" [Section 2(24)] means a company secretary as defined in clause (c) of sub-section (1) of Section 2 of the Company Secretaries Act, 1980 who is appointed by a company to perform the functions of a company secretary under the Companies Act, 2013.

"Company Secretary in practice" [Section 2(25)] means a company secretary who is deemed to be in practice under sub-section (2) of Section 2 of the Company Secretaries Act, 1980.

"Key Managerial Personnel" [Section 2(51)] in relation to a company, means—

- (i) the Chief Executive Officer or the managing director or the manager;
- (ii) the company secretary;
- (iii) the whole-time director;
- (iv) the Chief Financial Officer; -
- (v) such other officer, not more than one level below the directors who is in whole-time employment, designated as key managerial personnel by the Board; and
- (vi) such other officer as may be prescribed.

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

According to the above definition, a manager is an individual person. Such person is given the charge of whole or substantially the whole of managing the affairs of a company. Therefore, a person appointed as manager to head one of the sections of the company (say, marketing department) cannot be said to be a 'manager' within the meaning of Section 2 (53). **A manager functions under the superintendence, control and direction of the Board of Directors.**

It is not necessary that a manager should also be a director of the company though there is no restriction in designating a director as manager of the company. It is not permitted by Section 196(1)

for a company to appoint both managing director and manager at the same time. The simple reason behind this restriction is that when a person is entrusted with whole or substantially the whole of management, how can there be appointed another person for the same purpose. Moreover, due to overlapping of authorities between two powerful persons, the affairs of a company shall not be conducted the way they should, leading to mismanagement.

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

On simplifying we can understand, Managing Director means a **director** who is entrusted with **substantial powers of management** of the affairs of the company by:

- (i) virtue of the articles of a company, or
- (ii) an agreement with the company, or
- (iii) a resolution passed in its general meeting, or by its Board of Directors,

and includes a director occupying the position of the managing director, by whatever name called.

Explanation to Section 2(54) clarifies that **substantial powers of the management** shall not be deemed to include the power to do such administrative acts of a routine nature when so authorized by the Board such as:

(i)	the power to affix the common seal of the company to any document, or
(ii)	to draw and endorse any cheque on the account of the company in any bank, or
(iii)	to draw and endorse any negotiable instrument, or
(iv)	to sign any certificate of share, or
(v)	to direct registration of transfer of any share.

Thus, excluding the above administrative acts of a routine nature, the managing director enjoys substantial powers of conducting and managing the business of the company as per its memorandum and articles of association.

From the above definition, it emerges that a managing director needs to be a director in the first place. It is immaterial whether he is appointed as additional director or rotational director or non-rotational director. However, as soon as he ceases to be a director, he shall also cease to be a managing director.

It is not necessary that a director who occupies the position of the managing director needs to be called 'managing director'. He may be called by whatever name. The essential pre-requisite is that the director must be entrusted with substantial powers of management of the affairs of the company

excluding routine administrative acts as entrusted by the Board. If such is the case, the director is a managing director, by whatever name called. It may be noted that Section 196 (1) prohibits a company to appoint both managing director and manager at the same time. However, it shall be appropriate if a person is designated as a Managing Director instead of manager.

The Board of Directors exercises control over the managing director. Thus, powers as managing director are exercisable according to the directions of the Board.

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

As the definition suggests WTD is a director. Also, he is in the whole-time employment of the company *i.e.* he is a full-time employee who is required to devote his time in totality for the management of the company. A person who is not a director in the company cannot be employed as whole-time director.

Remuneration [Section 2 (78)]: 'Remuneration' means any money or its equivalent given or passed to any person for services rendered by him and **includes perquisites** as defined under the Income-Tax Act, 1961.



2. APPOINTMENT OF MANAGING DIRECTOR, WHOLE TIME DIRECTOR OR MANAGER [SECTION 196]

Section 196 of the Act contains the provisions for appointment of managing director, whole time director or manager. According to this section:

- (i) **Appointment [Section 196(1)]:** A company shall appoint or employ managing director, whole time director or manager. But a company shall not appoint or employ a managing director and a manager at the same time.

In other words, no company is permitted to appoint a manager if a managing director is already appointed and *vice-versa*. However, there can be both MD and whole-time director in a company.

- (ii) **Tenure [section 196(2)]:**
 - (a) No company shall appoint or re-appoint any person as its managing director, whole-time director or manager for a term exceeding **five years** at a time.
 - (b) It is further provided that no re-appointment shall be made earlier than one year before the expiry of his term.

Example 1: 'X' was appointed as Managing Director for life by the Articles of Association of a private company which was incorporated on 1st June, 2019. Section 196(2) of the Companies Act, 2013 lays down that no company shall appoint or re-appoint any person as its managing director, whole-time director or manager for a term exceeding five years at a

time. No concession or exception is allowed by the Act to private companies. Hence, 'X' cannot be appointed as managing director for life .

- (iii) **Eligibility Conditions for Appointment:** For appointing a person as a managing director, whole-time director or manager, firstly he shall not be disqualified for appointment as a director under section 164.

As per section 196(3), no company shall appoint or continue the employment of any person as managing director, whole-time director or manager who-

- (a) is below the age of 21 years or has attained the age of 70 years.

Requirement of Special Resolution for appointment of a person above the age of 70 years: There is a relaxation in case of a person above the age of 70 years. Accordingly, where a person has attained the age of seventy years, he may still be appointed to such office if a special resolution is passed in this respect. In such a case, the explanatory statement annexed to the notice for such motion shall indicate the justification for appointing such person.

Government approval required if no Special Resolution is passed: Further, where no such special resolution is passed but votes cast in favour of the motion exceed the votes, if any, cast against the motion and the Central Government is satisfied, on an application made by the Board, that such appointment is most beneficial to the company, the appointment of the person who has attained the age of seventy years may be made.

In other words, approval of the Central Government is required if special resolution could not be passed. The significance of this provision lies in the fact that because majority of the members were in favour of such appointment, their wish should not be turned down simply due to non-passing of special resolution. Thus, the appointment can be regularized by seeking approval of the Central Government, which, if satisfied, can accord such approval.

- (b) is an undischarged insolvent or has at any time been adjudged as an insolvent; or
- (c) has at any time suspended payment to his creditors or makes, or has at any time made, a composition with them; or
- (d) has at any time been convicted by a court of an offence and sentenced for a period of more than six months.
- (e) **Additional eligibility conditions for appointment as per Schedule V:** Part I of Schedule V¹ to the Companies Act, 2013, has prescribed additional eligibility

¹ Heading of Part I of Schedule V reads as 'Conditions to be fulfilled for the appointment of a Managing or Whole-time director of a manager without the approval of the Central Government'.

conditions for appointment as managing director or whole-time director or a manager without seeking approval from the Central Government. They are stated as under:

- (1) he had not been sentenced to imprisonment for any period, or to a fine exceeding one thousand rupees, for the conviction of an offence under 19 Acts² as specified under Part I of Schedule V.
- (2) he had not been detained for any period under the Conservation of Foreign Exchange and Prevention of Smuggling Activities Act, 1974 (COFEPOSA).

However, where the Central Government has given its approval to the appointment of a person convicted or detained under para (1) or para (2), as the case may be, no further approval of the Central Government shall be necessary for the subsequent appointment of that person if he had not been so convicted or detained subsequent to such approval.

- ³(3) he has completed the age of twenty-one years and has not attained the age of seventy years.

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

² The 19 Acts are:

- (i) the Indian Stamp Act, 1899.
- (ii) the Central Excise Act, 1944.
- (iii) the Industries (Development and Regulation) Act, 1951.
- (iv) the Prevention of Food Adulteration Act, 1954.
- (v) the Essential Commodities Act, 1955.
- (vi) the Companies Act, 2013 or any previous company law (Substituted by notification dated 12th September 2016)
- (vii) the Securities Contracts (Regulation) Act, 1956.
- (viii) the Wealth-tax Act, 1957.
- (ix) the Income-tax Act, 1961.
- (x) the Customs Act, 1962.
- (xi) the Competition Act, 2002.
- (xii) the Foreign Exchange Management Act, 1999.
- (xiii) the Sick Industrial Companies (Special Provisions) Act, 1985.
- (xiv) the Securities and Exchange Board of India Act, 1992.
- (xv) the Foreign Trade (Development and Regulation) Act, 1922.
- (xvi) the Prevention of Money-Laundering Act, 2002.
- (xvii) the Insolvency and Bankruptcy Code, 2016.
- (xviii) the Goods and Services Tax Act, 2017.
- (xix) the Fugitive Economic Offenders Act, 2018.

³ This condition is also specified by Section 196 (3) and mentioned earlier.

- (4) he is resident of India.

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

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

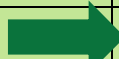
Explanation II clarifies that the condition above shall not apply to the companies in Special Economic Zones (SEZ).

However, a person, being a **non-resident in India** shall enter India only after obtaining a proper Employment Visa from the concerned Indian mission abroad. For this purpose, such person shall be required to furnish, along with the visa application form:

- profile of the company,
- the principal employer, and
- terms and conditions of such person's appointment.

(iv) **Procedure of Appointment [Section 196(4)]:**

Approval by Board and Shareholders	Approval by Central Government
Subject to the provisions of section 197 and Schedule V, a managing director, whole-time director or manager shall be appointed, and the terms and conditions of such appointment and remuneration payable shall be-	In case such appointment is at variance to the conditions specified in Part I of Schedule V, the appointment shall be approved by the Central Government.
 (i) approved by the Board of Directors at a meeting; and (ii) approved by shareholders by a resolution at the next general meeting of the company.	 Form MR-2 has been prescribed by Rule 7 of the <i>Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014</i> in which application for seeking approval from the Central Government shall be made within ninety days of such appointment of MD or WTD or manager in the company.

Inclusion of certain disclosures in Notice	 The notice convening Board or general meeting for considering such appointment shall include: (i) the terms and conditions of such appointment, remuneration payable, and (ii) such other matters including interest, of a director or directors in such appointments, if any.
Filing of Return:	 A return in the prescribed form⁴ along with the prescribed fee shall be filed with the Registrar within sixty days of such appointment.

- (v) **Validity of Acts [Section 196(5)]:** Subject to the provisions of this Act, where an appointment of a managing director, whole-time director or manager is not approved by the company at a general meeting, any act done by him before such approval shall be deemed to be valid.

Example 2: A Managing Director is appointed in the board meeting held on 20th May 2019. General meeting was to be held on 17th June, 2019 for approval of such appointment. Before the holding of general meeting, the managing director executed an agreement with another company of considerable importance on 3rd June, 2019. The general meeting was held accordingly on 17th June, 2019 but did not approve the appointment of managing director. Here, the agreement executed by Managing Director is valid. The acts done by the managing director from 20th May, 2019 to 17th June, 2019 i.e. upto the non-approval of his appointment by the shareholders at the general meeting, shall be valid subject to the provisions of the Companies Act, 2013.

Exemptions	
(i)	<i>In case of a Government Company, Section 196(2), (4) and (5) shall not apply. However, for availing the exemption, such Government Company must not have committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar. (Notification No. G.S.R. 463(E) dated 5th June, 2015 as amended by Notification No. G.S.R. 582 (E), dated 13-06-2017).</i>
(ii)	<i>In case of Private Company, Section 196(4) and (5) shall not apply provided such private company has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar. (Notification No. G.S.R. 464(E) dated 5th June, 2015 as amended by Notification No. G.S.R. 583(E) dated 5th June, 2015).</i>

⁴ Rule 3 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014 prescribes Form No. MR-1.

Example 3: Sukanya Limited, a company incorporated under the Companies Act, 2013, approved the appointment of Mr. Rajaram as the managing director of the company in the company's last annual general meeting. Accordingly, Mr. Rajaram was vested with the substantial powers of managing the business of the company. After a period of 1 year from the appointment of Mr. Rajaram, the company wants to employ Mr. Rakesh, the whole time employee of the company, as the manager of the finance department of the company. Now the company is in dilemma regarding the appointment of Mr. Rakesh.

In the said case, according to section 2(53) of the Companies Act, 2013, manager means an individual who, subject to the superintendence, control and direction of the Board of Directors, has the management of the whole, or substantially the whole, of the affairs of a Company, and includes a director or any other person occupying the position of a manager, by whatever name called, whether under a contract of service or not. According to the above definition, a manager is an individual person. Such person is given the charge of whole or substantially the whole of managing the affairs of a company. Therefore, a person appointed as manager to head any department of the company cannot be said to be a 'manager' within the meaning of section 2(53).

Further the provisions of section 196(1) of the Companies Act, 2013 applies to manager falling within the meaning of the definition of section 2(53)

In the given example, Mr. Rakesh is not falling within the meaning of the definition of section 2(53) and accordingly section 196(1) is not applicable. Hence company can go ahead with the appointment of Mr. Rakesh as manager of the Finance Department.

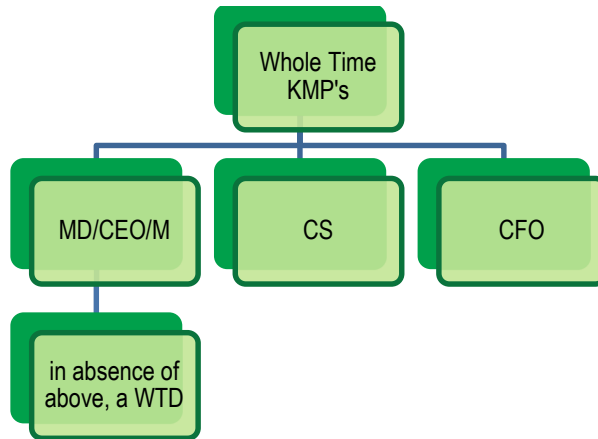
High Court of Bombay decided in *Sridhar Sundararajan v. Ultramarine & Pigments Limited* that Special resolution under section 196(3)(a) is to be passed to continue any person aged 70 years as MD even if his appointment was made before coming into force of Companies Act, 2013, i.e., before 1-4-2014 when he was below 70 years.



3. APPOINTMENT OF KEY MANAGERIAL PERSONNEL [SECTION 203]

Section 203 of the Act, and Rule 8 as well as Rule 8A of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014 contain the provisions for appointment of Key Managerial Personnel in the prescribed companies.

- (i) **Appointment of Key Managerial Personnel [Section 203(1)]:** Every company belonging to the prescribed class or classes of companies shall have the following whole time key managerial personnel:



According to **Rule 8** following companies shall have whole-time key managerial personnel:

- (a) every listed company; and
- (b) every other public company having a paid-up share capital of 10 crore rupees or more.

Requirement of Company Secretary in certain other companies: According to Rule 8A, every private company which has a paid up share capital of 10 crore rupees or more shall have a **whole-time company secretary**.

In other words, it is now mandatory for every private company to have a whole-time company secretary if its paid up share capital is 10 crore rupees or more.

(ii) Prohibition on individual to be appointed as Chairperson as well as Managing Director or Chief Executive Officer at the same time [Proviso to Section 203(1)]:

An individual shall not be appointed or reappointed as the Chairperson of the company, in pursuance of the articles of the company, as well as the Managing Director or Chief Executive Officer (CEO) of the company at the same time, **unless** —

- (a) the articles of such a company provide otherwise; or
- (b) the company does not carry multiple businesses. [First proviso to Section 203(1)]

Exemption from restriction: However, above-mentioned prohibition shall not apply to such class of companies which is engaged in multiple businesses and which has appointed one or more Chief Executive Officers for each such business as may be notified by the Central Government. [refer Second proviso to Section 203(1)]

In other words, a person appointed as Chairperson of a company cannot be appointed as MD or CEO at the same time in that company. This prohibition is not applicable in the following cases: [Second proviso to Section 203(1)]

- Where the articles of such company provide otherwise *i.e.*, they allow the Chairperson to be appointed as MD or CEO.

- Where the company belongs to the prescribed class of companies (*refer Box below*); is engaged in multiple businesses; and has appointed Chief Executive Officer for each such business.

Notified Public Companies: The MCA vide Notification No. S.O. 1913(E) dated 25th July, 2014 has notified that public companies having paid-up share capital of 100 crore rupees or more and annual turnover of 1,000 crore rupees or more which are engaged in multiple businesses and have appointed Chief Executive Officer for each such business shall be the class of companies for the purposes of the second proviso to sub-section (1) of section 203.

Explanation-For the purpose of this notification, the paid-up share capital and the annual turnover shall be decided on the basis of the latest audited balance sheet.

(iii) Conditions for Appointment:

- Requirement of Board Resolution⁵:** Every whole-time key managerial personnel of a company shall be appointed by means of a resolution of the Board. The resolution shall contain the terms and conditions of the appointment including the remuneration. [refer Section 203 (2)]
- Bar on multiple appointments:** A whole-time key managerial personnel shall not hold office in more than one company at the same time **except in its subsidiary company**. [Section 203 (3)]

However, key managerial personnel shall not be disentitled from being a director in any company with the permission of the Board. [refer Proviso to Section 203 (3)]

Provided further that whole-time key managerial personnel holding office in more than one company at the same time on the date of commencement of this Act, shall, within a period of six months from such commencement, choose one company, in which he wishes to continue to hold the office of key managerial personnel.

- Managing Director or Manager in more than one company [Third Proviso to Section 203(3)]:** If a person is MD or manager in some other company it is permissible for a company to appoint him as its managing director. The *modus operandi* is as under:

⁵ Rule 8 of the Companies (Meetings of Board and its Powers) Rules, 2014 requires passing of Board Resolution at a meeting of the Board if a key managerial personnel is appointed (or removed).

Person so appointed /employed as MD

- should be MD/M in one company, and of not more than one other company
- made/approved by Board resolution
- passed with the consent of all the directors present at the meeting
- specific notice of such meeting, and of the resolution to be moved thereat has been given to all the directors then in India.

Example 4: Virasat Limited, a company incorporated under the Companies Act, 2013, has a board of directors consisting of 10 directors, wants to appoint Mr. Vakharia as its Managing Director (MD) in the upcoming Annual General Meeting (AGM). Mr. Vakharia is already serving as the MD of other public company. Accordingly, for the appointment of Mr. Vakharia specific notice for the board meeting and the resolution to be moved thereat has been given to all the directors. The resolution for the appointment of Mr. Vakharia has been passed at the board meeting. Out of 8 directors present, 6 directors voted in favour of the resolution and the remaining 2 directors refrained from voting. Thereafter, the company approved the appointment of Mr. Vakharia in the AGM. Here in the given instance, appointment of Mr. Vakharia is not valid in law as the resolution is not passed by all the directors present in the board meeting.

- (v) **Filling of Vacancy of Key Managerial Personnel (KMP) [Section 203(4)]:** If the office of any whole-time KMP is vacated, the resulting vacancy shall be filled-up by the Board at a meeting of the Board within a period of six months from the date of such vacancy.
- (vi) **Penalty for non-compliance [Section 203(5)]:**
- Company:** If any company makes any default in complying with the provisions of this section, such company shall be liable to a penalty of 5 Lakh rupees.
 - Director and KMP:** Every defaulting director and KMP shall be liable to a penalty of 50,000 rupees. Where the default is a continuing one, they shall be liable with a further penalty of 1,000 rupees for each day after the first during which such default continues but not exceeding 5 Lakh rupees.

Exemptions

*In case of **Government companies**, after sub-section (4) of Section 203, the following sub-section shall be inserted vide Notification No. G.S.R. 463(E), dated 5th June, 2015 as amended by Notification No. G.S.R. 582 (E), dated 13th June, 2017, namely:*

“(4A) The provisions of sub-section (1), (2), (3) and (4) of this section shall not apply to a managing director or Chief Executive Officer or manager and in their absence, a whole-time director of the Government company.”

*The sub-section (4A) shall be applicable to a **Government company** only if it has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar.*

In a decision given by National Company Law Tribunal, Kolkata Bench in *Usha Martin Telematics Ltd., In re*, it was held that where Tribunal had already compounded offences for company in respect of appointment of CFO and CS, application of Ex-Directors & Managers seeking compounding of offence, was to be allowed.

In the said case in financial year 2014-15, company's paid up capital was Rs. 197.60 crores and still, company had not appointed CFO and CS and, thus, violated provisions of section 203(1)(iii). Subsequent to show cause notice, company appointed CFO and CS. Form DIR-12 was filed in relation to such appointment. Applicants ex-directors and ex-managers admitted offence and thus, filed instant application seeking compounding of offence under section 441 of the Companies Act, 2013. Here the Tribunal held liable to ex-directors and managers for alleged offence only for period for which such applicants were directors/officers in company. Even where tribunal had already compounded offence for company, application by ex-directors and managers of company seeking compounding of offence was also to be allowed.



4. FUNCTIONS OF COMPANY SECRETARY [SECTION 205]

The provisions of Section 205 of the Act are stated as under:

(i) **Functions to be performed by Company Secretary:** According to Section 205 (1) and Rule 10 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014, a Company Secretary shall perform the following functions:

- (a) **to report to the Board about compliance with the provisions of the Companies Act, 2013**, the rules made thereunder and other laws applicable to the company;
- (b) to ensure that the company **complies with the applicable secretarial standards**;
- (c) to provide to the directors of the company, collectively and individually, such **guidance** as they may require, with regard to their duties, responsibilities and powers;
- (d) to facilitate the convening of **meetings** and attend Board, committee and general meetings and **maintain the minutes** of these meetings;
- (e) to **obtain approvals** from the Board, general meeting, the government and such other authorities as required under the provisions of the Companies Act, 2013;
- (f) to **represent before various regulators**, and other authorities under the Companies Act, 2013 in connection **with discharge of various duties** under the said Act;
- (g) to **assist the Board in the conduct of the affairs** of the company;
- (h) to **assist and advise the Board in ensuring good corporate governance** and in complying with the corporate governance requirements and best practices; and
- (i) to discharge such **other duties** as have been specified under the Companies Act, 2013 or the Rules made thereunder; and
- (j) **such other duties as may be assigned by the Board** from time to time.

Functions performed by CS

report to board about compliance of Companies Act	ensure company complies applicable SS's	guidance to directors w.r.t. their duties, responsibilities and powers	convening and attending and maintaining minutes of meetings	obtains approvals	represent w.r.t discharge of various duties	assist board in conduct of affairs	assist & advice board in complying with corporate governance	other duties as assigned by board

Clarification: The expression “secretarial standards” means secretarial standards issued by the Institute of Company Secretaries of India constituted under section 3 of the Company Secretaries Act, 1980 and approved by the Central Government. Under Section 118 (10) of the Act, the Central Government has approved SS-1 (Secretarial Standard on Meetings of the Board of Directors) and SS-2 (Secretarial Standard on General Meetings).

(ii) **No effect on duties and functions of certain important functionaries:** According to Section 205 (2), the provisions contained in Section 204 relating to the ‘secretarial audit for bigger companies’ and Section 205 relating to the ‘functions of company secretary’ shall not affect the duties and functions of the Board of Directors, Chairperson of the company, Managing Director or Whole-time Director under this Act, or any other law for the time being in force.

In other words, these important functionaries of the company cannot be absolved of their duties and functions simply because a secretarial audit has been conducted or certain functions have been assigned to the company secretary. They shall always remain responsible to the company and in no way their responsibility shall be reduced.



5. COMPANY TO FIX LIMIT WITH REGARD TO REMUNERATION [SECTION 200]

Section 200 of the Act is instructive in nature. According to this section, a company needs to take care of certain parameters and may adopt an administrative ceiling as it may deem fit within the statutory ceiling with regard to fixing of managerial remuneration where it has inadequate or no profits. However, effective from 12-09-2018 in such cases the company is not required to seek any approval from the Central Government.

Section 200 states that notwithstanding anything contained in this Chapter, a company may, while according its approval under Section 196 to any appointment or to any remuneration under Section 197 in respect of cases where the company has inadequate or no profits, fix the remuneration within the limits specified in this Act, at such amount or percentage of profits of the company, as it may deem fit.

While fixing such remuneration the company shall have regard to:

(a)	the financial position of the company;
(b)	the remuneration or commission drawn by the individual concerned in any other capacity;
(c)	the remuneration or commission drawn by him from any other company;
(d)	professional qualifications and experience of the individual concerned;
(e)	any other matters as may be prescribed. Parameters for consideration of remuneration In this respect, Rule 6 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014, prescribes that the company shall have regard to the following matters: (i) the Financial and operating performance of the company during the three preceding financial years. (ii) the relationship between remuneration and performance. (iii) the principle of proportionality of remuneration within the company, ideally by a rating methodology which compares the remuneration of directors to that of other directors on the board and employees or executives of the company. (iv) whether remuneration policy for directors differs from remuneration policy for other employees and if so, an explanation for the difference. (v) the securities held by the director, including options and details of the shares pledged as at the end of the preceding financial year.



6. OVERALL MAXIMUM MANAGERIAL REMUNERATION AND MANAGERIAL REMUNERATION IN CASE OF ABSENCE OR INADEQUACY OF PROFITS [SECTION 197]

Section 197 of the Act lays down the provisions relating to overall maximum managerial remuneration payable by every **public company** and the managerial remuneration payable by it in case of absence or inadequacy of profits. Section 197 read with Schedule V to the Companies Act,

2013 defines maximum remuneration payable to **KMPs and other directors**. This section does not apply to a private company. These provisions are discussed as under:

(i) **Overall Maximum Managerial Remuneration [Section 197(1)]**

- (a) Section I of Part II of Schedule V headed as 'Remuneration Payable by Companies having Profits' states that 'subject to the provisions of Section 197, a company having profits in a financial year may pay remuneration to a managerial personnel or persons or other director or directors not exceeding the limits specified in this section'. Accordingly, the overall managerial remuneration to the **Directors** including managing director, whole time director and manager in respect of any financial year is summarized as below:

S. No.	Conditions	Maximum remuneration payable by Public company to directors, including managing director and whole time director and manager in any financial year	When remuneration can be exceeded as referred to in column (b)
	(a)	(b)	(c)
(i)	Overall limit applicable to managerial remuneration	11% of the net profits of the company for that financial year Note: Net profits are to be calculated in accordance with Section 198 except that the remuneration payable to the directors shall not be deducted from the gross profits.	Subject to the provisions of Schedule V, the company in general meeting may authorize exceeding the overall limit of 11%.
(ii)	If there is one Managing director/ Whole time director/ manager i.e. Remuneration payable to one managing director/whole time director/manager	5% of the net profits of the company for that financial year.	This limit of 5% may be exceeded with the approval of the company in general meeting by passing a Special Resolution.
(iii)	If there is more than one	10% of the net profits of	This limit of 10% may be

	Managing Director/ Whole time director/manager i.e. Remuneration payable to all such Managing Director/Whole time Director/Manager taken together	the company for that financial year.	exceeded with the approval of the company in general meeting by passing a Special Resolution.
(iv)	Remuneration payable to directors who are neither Managing Directors nor Whole time directors	1% of the net profits of the company if there is a Managing Director or a Whole time director	This limit of 1% may be exceeded with the approval of the company in general meeting by passing a Special Resolution.
(v)	Remuneration payable to directors who are neither Managing Directors nor Whole time directors	3% of the net profits of the company provided there is no Managing Director or Whole time director	This limit of 3% may be exceeded with the approval of the company in general meeting by passing a Special Resolution.

Instances to obtain prior approval in case of default: It is to be noted that where the company has defaulted in payment of dues to any bank or public financial institution or non-convertible debenture holders or any other secured creditor, prior approval of such person (as applicable) shall have to be obtained by the company before obtaining the approval in the general meeting.

Exclusion of sitting fees: Section 197(2) provides that above percentages shall be exclusive of any fees payable to directors under section 197(5).

- (b) Section 197(8) provides that the net profits shall be computed in the manner laid down in section 198. This stipulation is already covered by Section 197 (1) which further provides that the remuneration of the directors shall not be deducted from the gross profits.

(ii) No profits or inadequate profits [Section 197(3) & (11)]

- (a) If in any financial year, a company has no profits or its profits are inadequate, the company shall not pay by way of remuneration any sum (exclusive of sitting fees) to its directors, including any managing or whole- time director or manager or any other non-executive director including an independent director, except in accordance with the provisions of Schedule V.
- (b) In cases where Schedule V is applicable on grounds of no profits or inadequate profits,

any provision relating to the remuneration of any director which purports to increase or has the effect of increasing the amount thereof, shall not have any effect unless such increase is in accordance with the conditions specified in that Schedule.

Accordingly the following provisions which purport to increase or has the effect of increasing the remuneration payable to directors shall not have any effect unless are in accordance with the conditions specified in that schedule:

- ✓ the provision contained in the memorandum or articles of the company, or
- ✓ in an agreement entered into by the company, or
- ✓ in any resolution passed by the company in general meeting or its Board.

SECTION II OF PART II OF SCHEDULE V- Remuneration payable by companies having no profit or inadequate profit

Where in any financial year during the currency of tenure of a managerial person, a company has no profits or its profits are inadequate, it may pay remuneration to the managerial person or other director not exceeding the limits under (A) and (B) given below:

Limits under (A):

(1)	(2)	(3)
Where the effective capital is (in any FY)	Limit of yearly remuneration payable shall not exceed (in any FY) in case of managerial remuneration	Limit of yearly remuneration payable shall not exceed (in any FY) in case of other directors
(i) Negative or less than ₹ 5 crores	₹ 60 lakhs	₹ 12 lakhs
(ii) ₹ 5 crores and above but less than ₹ 100 crores	₹ 84 lakhs	₹ 17 lakhs
(iii) 100 crores and above but less than ₹ 250 crores	₹ 120 lakhs	₹ 24 lakhs
(iv) ₹ 250 crores and above	₹ 120 lakhs plus 0.01% of the effective capital in excess of ₹ 250 crores	₹ 24 Lakhs plus 0.01% of the effective capital in excess of ₹ 250 crores:]"

However, the remuneration in excess of above limits may be paid if the resolution passed by the shareholders is a special resolution.

Explanation 1.—For the purposes of Section II of this Part, “**effective capital**” means the aggregate of the paid-up share capital (excluding share application money or advances against shares); amount, if any, for the time being standing to the credit of share premium account; reserves and surplus (excluding revaluation reserve); long-term loans and deposits repayable after one year (excluding working capital loans, over drafts, interest due on loans unless funded, bank guarantee, etc., and other short-term arrangements) as reduced by the aggregate of any investments (except in case of investment by an investment company whose principal business is acquisition of shares, stock, debentures or other securities), accumulated losses and preliminary expenses not written off.

Explanation 2. —

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

Explanation 3- It is hereby clarified that for a period less than one year, the limits shall be pro-rated.

Thus, if a managerial person is employed for a part of the year, the remuneration payable to him shall be pro-rated.

Limits under (B):

In case of a managerial person or other director who is functioning in a **professional capacity**, remuneration as per item (A) may be paid, if such managerial person or other director:

- is not having any interest in the capital of the company or its holding company or any of its subsidiaries directly or indirectly or through any other statutory structures (*i.e. does not hold any shares subject to the deeming provision below*);

Note: “Statutory Structure” means any entity which is entitled to hold shares in any company formed under any statute.

- is not having any, direct or indirect interest or related to the directors or promoters of the company or its holding company or any of its subsidiaries at any time during the last two years before or on or after the date of appointment;
- possesses graduate level qualification with expertise and specialised knowledge in the field in which the company operates:

Deeming provision as to the holding of shares: It is provided that any employee of a company holding shares of the company not exceeding 0.5% of its paid-up share capital under any scheme formulated for allotment of shares to such employees including Employees Stock Option Plan or by way of qualification shall be deemed to be a person not having any interest in the capital of the company.

Applicable conditions for payment of remuneration: The limits specified under items (A) and (B) above shall apply, if-

- (i) payment of remuneration is approved by a resolution passed by the Board and, in the case of a company covered under Section 178 (1), also by the Nomination and Remuneration Committee;
- (ii) the company has not committed any default in payment of dues to any bank or public financial institution or non-convertible debenture holders or any other secured creditor, and in case of default, the prior approval of the bank or public financial institution concerned or the non-convertible debenture holders or other secured creditor, as the case may be, shall be obtained by the company **before obtaining the approval in the general meeting**;
- (iii) an ordinary resolution or a special resolution, as the case may be, has been passed for payment of remuneration as per item (A) or a special resolution has been passed for payment of remuneration as per item (B), at the general meeting of the company for a period **not exceeding three years**.
- (iv) a statement along with a notice calling the general meeting referred to in clause (iii) is given to the shareholders containing the following information, namely:
 - I. General information:
 - (1) Nature of industry
 - (2) Date or expected date of commencement of commercial production
 - (3) In case of new companies, expected date of commencement of activities as per project approved by financial institutions appearing in the prospectus
 - (4) Financial performance based on given indicators
 - (5) Foreign investments or collaborations, if any.
 - II. Information about the appointee:
 - (1) Background details
 - (2) Past remuneration
 - (3) Recognition or awards

- (4) Job profile and his suitability
 - (5) Remuneration proposed
 - (6) Comparative remuneration profile with respect to industry, size of the company, profile of the position and person (in case of expatriates the relevant details would be with respect to the country of his origin)
 - (7) Pecuniary relationship directly or indirectly with the company, or relationship with the managerial personnel or other director, if any.
- III. Other information:
- (1) Reasons of loss or inadequate profits
 - (2) Steps taken or proposed to be taken for improvement
 - (3) Expected increase in productivity and profits in measurable terms
- IV. Disclosures: The following disclosures shall be mentioned in the Board of Director's report under the heading "Corporate Governance", if any, attached to the Financial statement:
- (i) all elements of remuneration package such as salary, benefits, bonuses, stock options, pension, etc., of all the directors;
 - (ii) details of fixed component and performance linked incentives along with the performance criteria;
 - (iii) service contracts, notice period, severance fees; and
 - (iv) stock option details, if any, and whether the same has been issued at a discount as well as the period over which accrued and over which exercisable.

(iii) Determination of Remuneration [Section 197(4)]

- (a) The remuneration payable to the directors of a company, including any managing or whole-time director or manager, shall be determined, in accordance with and subject to the provisions of this section, either
 - (i) by the articles of the company, or
 - (ii) by a resolution or,
 - (ii) if the articles so require, by a special resolution, passed by the company in general meeting, and
- (b) The remuneration payable to a director determined aforesaid shall be inclusive of the remuneration payable to him for the services rendered by him in any other capacity.

- (c) Any remuneration for services rendered by any such director in other capacity shall not be so included if—
- (1) the services rendered are of a professional nature; and
 - (2) in the opinion of the Nomination and Remuneration Committee, if the company is covered under Section 178 (1), or in the opinion of the Board of Directors in other cases, the director possesses the requisite qualification for the practice of the profession.

Simply stated, the Board of Directors cannot determine the remuneration payable to the directors. The remuneration shall be determined (subject to the provisions of Section 197) by the articles or by a resolution or if required by the articles, by passing a special resolution.

However, besides remuneration, a director may be paid some other remuneration if he provides professional services to the company and further, in the opinion of the Nomination and Remuneration Committee (if the company has formed such committee) or in the opinion of the Board of Directors (where no such committee exists) the director possesses the requisite qualification for practicing his profession.

Example 5: Star Health Specialties Ltd. owns a Multi-Specialty Hospital in Chennai. Dr. Hamilton, a practicing Heart Surgeon, has been appointed by the company as its director and it wants to pay him fee, on case to case basis, for surgery performed on the patients at the hospital.

In the given **example**, as Dr. Hamilton has been appointed as a director. He has to be paid a fee for surgeries performed by him. It is to be noted that such payment is permissible under Section 197(4) which states that the remuneration payable to the directors including managing or whole-time director or manager shall be inclusive of the remuneration payable for the services rendered by him in any other capacity except the following:

- (a) the services rendered are of a professional nature; and
- (b) in the opinion of the Nomination and Remuneration Committee (if applicable) or the Board of Directors in other cases, the director possesses the requisite qualification for the practice of the profession.

The company, therefore, can pay extra remuneration to Dr. Hamilton like professional fee for surgeries performed by him in his professional capacity; and such payment shall not be construed as managerial remuneration under the Act.

(iv) Sitting Fees to Directors [Section (5)]:

- (a) **Fees for attending meeting:** A director may receive remuneration by way of fee for attending meetings of the Board or Committee thereof or for any other purpose whatsoever as may be decided by the Board subject to the conditions imposed by Rule

4 of the Companies (Appointment and Remuneration of Managerial personnel) Rules, 2014 as under:

- The sitting fees shall not exceed one lakh rupees per meeting of the Board or committee thereof. [As per Rule 4]
- The sitting fee payable to the Independent Directors and Women Directors shall not be less than that payable to other directors. [As per Proviso to Rule 4]

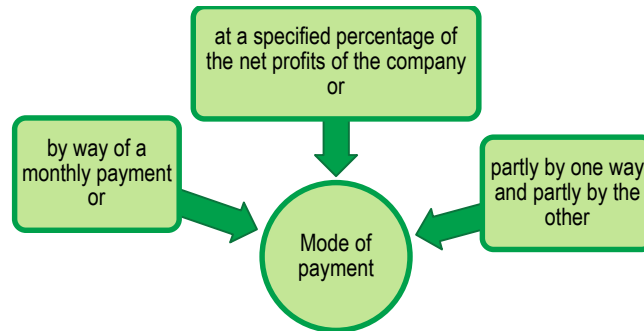
Note: According to Section 197 (2), the percentages mentioned under Section 197 (1) shall be **exclusive of any sitting fees** payable to directors for attending meetings of the Board or committee thereof or for any other purpose whatsoever as may be decided by the Board.

- (b) **Scale of fees may differ:** Different fees for different classes of companies and fees in respect to independent directors may be such as may be prescribed.

Example 6: The Articles of Association of a listed company have fixed payment of sitting fee for each Meeting of Directors subject to a maximum of ₹ 30,000. In view of the increased responsibilities of the independent directors of listed companies, the company proposes to increase the sitting fee to ₹ 45,000 per meeting. W.r.t. to the said proposal, Section 197(5) of the Companies Act, 2013 provides that a director may receive remuneration by way of fee for attending the Board/Committee meetings or for any other purpose as may be decided by the Board provided that the amount of such fees shall not exceed the prescribed amount. As per Rule 4 of the Companies (Appointment and Remuneration of Managerial personnel) Rules, 2014 the amount of sitting fees payable for attending meetings of the Board or Committees thereof may be decided by the Board but such sitting fees shall not exceed 1 lakh rupee per meeting. Further, the sitting fee payable to an independent director shall not be less than that payable to other directors.

From the above, it is clear that sitting fees can be increased from 30,000 rupees to 45,000 rupees per meeting by passing a resolution in the Board Meeting and altering the Articles of Association by passing a Special Resolution. When sitting fees stands increased for other directors, it shall automatically be increased in case of independent directors because the latter cannot be paid less than that payable to former.

- (v) **Mode of payment of Remuneration [Section 197(6)]:** A director or manager may be paid remuneration in any of the following manner:



The term used in Section 197 (6) is 'director' which may be taken to mean all types of directors *i.e.* MD or whole-time director or executive/non-executive director. Further, remuneration can be paid on monthly basis or on the basis of specified percentage of the net profits. Even, a combination of both the methods may also be adopted.

- (vi) **Refund of excess remuneration if paid to a director [Section 197(9) and (10)]:** If any director draws or receives excess remuneration than the limit prescribed by Section 197 or without approval required under this section, such director shall:



Waiver, whether possible: The company shall not waive the recovery of any sum refundable to it under Section 197 (9). However, the waiver is possible only if it is approved by the company by passing a special resolution within two years from the date the sum becomes refundable.

Instances to obtain prior approval of waiver in case of default: It is to be noted that where the company has defaulted in payment of dues to any bank or public financial institution or non-convertible debenture holders or any other secured creditor, the prior approval of such person respectively shall be obtained by the company before obtaining approval of such waiver by a special resolution.

(vii) Disclosure in Board's Report by a Listed Company [Section 197(12) and Rule 5]

Every listed company shall disclose in the Board's report-

- ratio of the remuneration of each director to the median employee's remuneration
- other details given under rule 5
 - disclosure prescribed under section 197(12)
 - % increase in remuneration of each director, CFO, CEO, CS or manager in FY
 - % increase in the median remuneration of employees in the FY
 - no. of permanent employees on rolls of company
 - average percentile increase made in the salaries of employees other than managerial personnel in the last FY
 - affirmation of remuneration as per remuneration policy
- statement showing top 10 employees in terms of remuneration
 - employeeed through out FY
 - received remuneration in aggregate not less than 1.02 cr
 - employed for part of the FY
 - received remuneration in aggregate not less than 8.50 lakhs /month
 - employed throughout FY/part thereof
 - received remuneration aggregate not less than 2% of the equity shares of the company , or in excess of that drawn by MD/WTd/M +holds by himself/along his spouse +dependent children
- particulars of all the employees as per rule Rule 5(3) + whether such employee is a relative of any D/M

- (a) Every listed company shall disclose in the Board's report, the ratio of the remuneration of each director to the median employee's remuneration and other details as prescribed under Rule 5 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014.
- (b) According to Rule 5 (1) every listed company shall disclose in the Board's report:
 - (i) the ratio of the remuneration of each director to the median remuneration of the employees of the company for the financial year; this disclosure is also prescribed by Section 197 (12).
 - (ii) the percentage increase in remuneration of each director, Chief Financial Officer, Chief Executive Officer, Company Secretary or manager, if any, in the financial year;
 - (iii) the percentage increase in the median remuneration of employees in the financial year;
 - (iv) the number of permanent employees on the rolls of company;

- (v) average percentile increase already made in the salaries of employees other than the managerial personnel in the last financial year and its comparison with the percentile increase in the managerial remuneration and justification thereof and point out if there are any exceptional circumstances for increase in the managerial remuneration; and
- (vi) affirmation that the remuneration is as per the remuneration policy of the company.

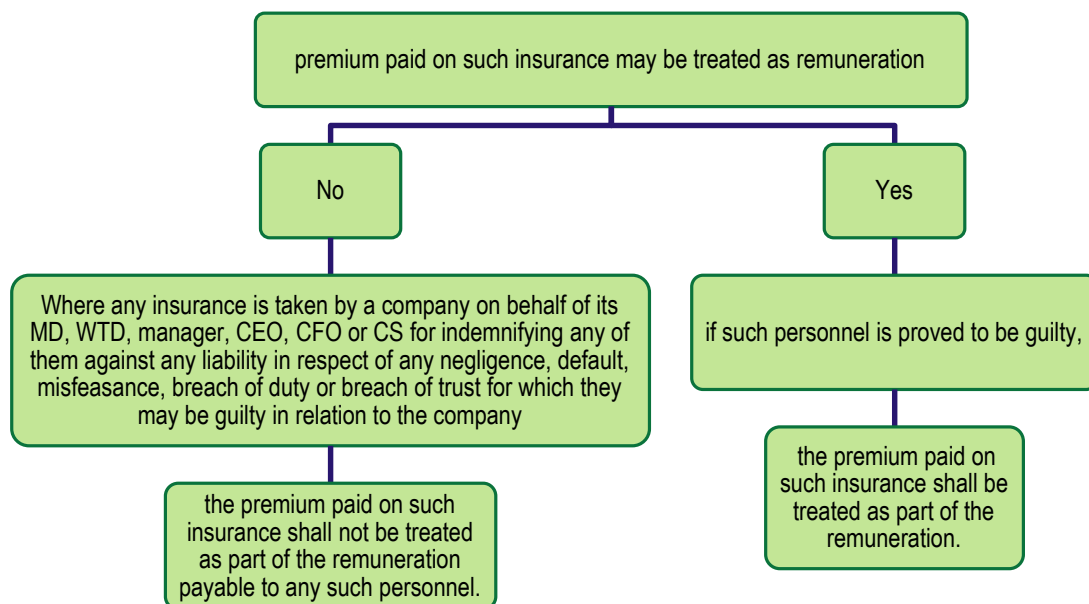
Meaning of median: (i) The expression “median” means the numerical value separating the higher half of a population from the lower half and the median of a finite list of numbers may be found by arranging all the observations from lowest value to highest value and picking the middle one;

(ii) if there is an even number of observations, the median shall be the average of the two middle values.

- (c) According to Rule 5 (2) the board’s report shall include a statement showing the **names of the top ten employees** in terms of remuneration drawn and the **name of every employee, who-**
 - (i) if employed throughout the financial year, was in receipt of remuneration for that year which, in the aggregate, was not less than one crore and two lakh rupees *i.e.* rupees 1.02 crore;
 - (ii) if employed for a part of the financial year, was in receipt of remuneration for any part of that year, at a rate which, in the aggregate, was not less than eight lakh and fifty thousand rupees per month;
 - (iii) if employed throughout the financial year or part thereof, was in receipt of remuneration in that year which, in the aggregate, or as the case may be, at a rate which, in the aggregate, is in excess of that drawn by the managing director or whole-time director or manager and holds by himself or along with his spouse and dependent children, not less than two percent of the equity shares of the company.
- (d) According to Rule 5 (3), the statement referred to in Rule 5 (2) [refer para (c) above] shall also indicate some particulars of the above employees like designation, remuneration received, nature of employment, qualification and experience, date of commencement of employment, age, last employment held by such employee before joining the company, the percentage of equity shares held by the employee in the company within the meaning of clause (iii) of Rule 5 (2) [refer para (c) (iii) above], and whether any such employee is a relative of any director or manager of the company and if so, name of such director or manager.

(viii) Premium paid in respect of Insurance taken for indemnification [Section 197(13)]:

Section 197 (13) deals with taking of insurance by a company on behalf of its MD, WTD, manager, CEO, CFO or CS and whether to treat the premium paid on such insurance as remuneration or not.

**(ix) Remuneration/Commission permissible from holding/subsidiary company [Section 197(14)]:**

If any director who is a managing or whole-time director receives any commission from the company, he shall not be disqualified from receiving any remuneration or commission from any holding company or subsidiary company of such company subject to the provisions of Section 197.

However, the requirement is that such fact must be disclosed by the company in the Board's report.

(x) Penalty for non-compliance [Section 197(15)]: Non-compliance with the provisions of Section 197 gives rise to following penalty:

- **Defaulting person:** liable to a penalty of rupees one lakh.
- **Company:** liable to a penalty of rupees five lakhs.

(xi) Auditors' report to contain a statement regarding remuneration [Section 197(16)]: The auditor of the company shall, in his report under section 143, make a statement regarding remuneration as under:

- whether the remuneration paid by the company to its directors is in accordance with the provisions of Section 197;
- whether remuneration paid to any director is in excess of the limit laid down under Section 197; and
- give such other details as may be prescribed.

(xii) **Application pending with Central Government as on 12-09-2018 [Section 197(17)]:** On and from the commencement of the Companies (Amendment) Act, 2017, any application made to the Central Government under the provisions of Section 197 [as it stood before such commencement i.e. before 12-09-2018], which is pending with that Government shall abate, and the company shall, within one year of such commencement, obtain the approval in accordance with the provisions of this section, as so amended.

In other words, in case of pendency of any application as on 12-09-2018, the company shall obtain the approval from the Central Government according to the amended Section 197 within one year from this date.

Exemptions/Modifications

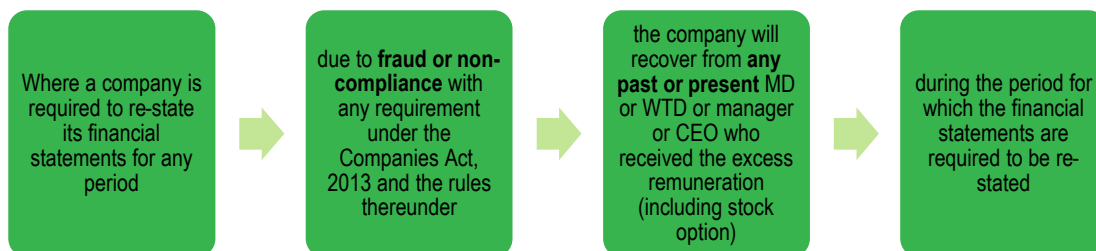
- (i) In case of **Government Companies**, Section 197 shall not apply. However, for availing the exemption, such Government Company must not have committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar. (Notification No. G.S.R. 463(E) dated 5th June, 2015 as amended by Notification No. G.S.R. 582 (E), dated 13-06-2017).
- (ii) In case of **Nidhi Company**, second proviso to sub-section (1) of section 197 shall apply with the modification that the remuneration of a director who is neither managing director nor whole-time director or manager for performing special services to the Nidhis specified in the articles of association may be paid by way of monthly payment subject to the approval of the company in general meeting and also to the provisions of section 197:
- Provided that no approval of the company in general meeting shall be required where,
- a Nidhi does not have a managing director or a whole-time director or a manager;
 - the remuneration payable during a financial year to all the directors of the Nidhi does not exceed ten per cent. of the net profits of such Nidhi or fifteen lakh rupees, whichever is less; and
 - a remuneration payable under clause (b) is approved by a special resolution passed in this behalf by the Nidhi.

Note: while availing the above modification, the Nidhi Company shall ensure that the interests of their shareholders are protected. (Notification No. G.S.R. 465(e) dated 5th June, 2015)



7. RECOVERY OF MANAGERIAL REMUNERATION IN CERTAIN CASES [SECTION 199]

Section 199 of the Act provides for recovery of managerial remuneration in following case-



The excess remuneration to be recovered shall be the difference between actual amount of remuneration received by such person and the remuneration that would have been payable to him as per restatement of financial statements.

Liability of the defaulter: The recovery of remuneration does not prejudice (*i.e.* impair) any liability that may be incurred under the provisions of the Companies Act, 2013 or any other law for the time being in force. In other words, the defaulting person because of whom fraud or non-compliance took place and the financial statements were restated at that time, even though has repaid excess remuneration, shall not escape from any liability that may be incurred under the provisions of the Companies Act, 2013 or any other law.



8. CALCULATION OF PROFITS [SECTION 198]

According to Section 198 of the Act, net profits for any financial year for the purpose of managerial remuneration payable under section 197 shall be calculated as follows:



(i) Credit shall be given for the sums specified in Section 198(2)

Add: Bounties and subsidies received from any Government, or any public authority constituted or authorised in this behalf, by any Government, unless and except in so far as the Central Government otherwise directs.

(ii) Credit shall not be given for those sums specified in Section 198(3)

Less: (if credited to the P & L A/c for arriving at profit before tax)

- (a) profits, by way of premium on shares or debentures of the company, which are issued or sold by the company unless the company is an investment company as referred to in clause (a) of the Explanation to section 186;
- (b) profits on sales by the company of forfeited shares;
- (c) profits of a capital nature including profits from the sale of the undertaking or any of the undertakings of the company or of any part thereof;

- (d) profits from the sale of any immovable property or fixed assets of a capital nature comprised in the undertaking or any of the undertakings of the company, unless the business of the company consists, whether wholly or partly, of buying and selling any such property or assets:

Provided that where the amount for which any fixed asset is sold exceeds the written-down value thereof, credit shall be given for so much of the excess as is not higher than the difference between the original cost of that fixed asset and its written-down value;

- (e) any change in carrying amount of an asset or of a liability recognized in equity reserves including surplus in profit and loss account on measurement of the asset or the liability at fair value.
- (f) any amount representing unrealized gains, notional gains or revaluation of assets.

(iii) In making the computation aforesaid, the following sums specified under Section 198(4) shall be deducted,

- (a) all the usual working charges;
- (b) directors' remuneration;
- (c) bonus or commission paid or payable to any member of the company's staff, or to any engineer, technician or person employed or engaged by the company, whether on a whole-time or on a part-time basis;
- (d) any tax notified by the Central Government as being in the nature of a tax on excess or abnormal profits;
- (e) any tax on business profits imposed for special reasons or in special circumstances and notified by the Central Government in this behalf;
- (f) interest on debentures issued by the company;
- (g) interest on mortgages executed by the company and on loans and advances secured by a charge on its fixed or floating assets;
- (h) interest on unsecured loans and advances;
- (i) expenses on repairs, whether to immovable or to movable property, provided the repairs are not of a capital nature;
- (j) outgoings inclusive of contributions made under section 181 (Company to contribute to bona fide and charitable funds);
- (k) depreciation to the extent specified in section 123;
- (l) the excess of expenditure over income, which had arisen in computing the net profits in accordance with this section in any year which begins at or after the commencement

of this Act, in so far as such excess has not been deducted in any subsequent year preceding the year in respect of which the net profits have to be ascertained;

- (m) any compensation or damages to be paid in virtue of any legal liability including a liability arising from a breach of contract;
- (n) any sum paid by way of insurance against the risk of meeting any liability such as is referred to in clause (m);
- (o) debts considered bad and written off or adjusted during the year of account.

(iv) In making the computation aforesaid, the following sums specified under Section 198(5) shall not be deducted:

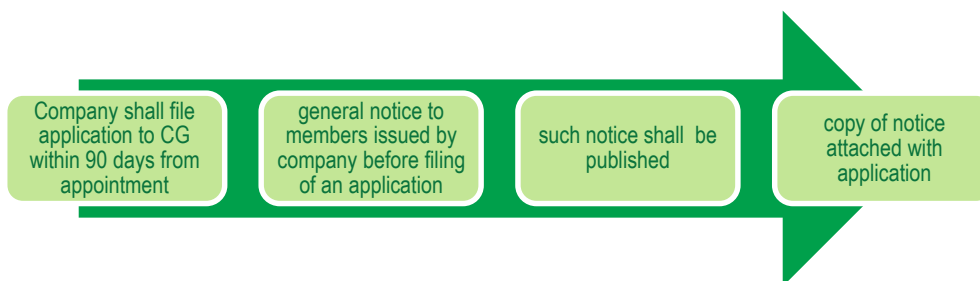
- (a) income-tax and super-tax payable by the company under the Income-tax Act, 1961, or any other tax on the income of the company not falling under clauses (d) and (e) of sub-section (4);
- (b) any compensation, damages or payments made voluntarily, that is to say, otherwise than in virtue of a liability such as is referred to in clause (m) of sub-section (4);
- (c) loss of a capital nature including loss on sale of the undertaking or any of the undertakings of the company or of any part thereof not including any excess of the written-down value of any asset which is sold, discarded, demolished or destroyed over its sale proceeds or its scrap value;
- (d) any change in carrying amount of an asset or of a liability recognised in equity reserves including surplus in profit and loss account on measurement of the asset or the liability at fair value.



9. FORMS OF, AND PROCEDURE IN RELATION TO, CERTAIN APPLICATIONS [SECTION 201]

Section 201 of the Act contains provisions which need to be followed for seeking approval from the Central Government if an application is made under Section 196 for the appointment of a person as Managing Director who has attained the age of seventy years but in whose case the appointment could not be regularised by passing a special resolution though votes cast in favour of the motion exceeded the votes cast against the motion. Non-passing of special resolution as before also contravenes Schedule V. Accordingly, for regularizing the appointment the company would apply to the Central Government for approval based on the fact that majority of the shareholders are in favour of such appointment as they find this appointment to be most beneficial to the company. It may be noted that now no approval is required for managerial remuneration in any case.

The process for seeking approval as given in Section 201 and Rule 7 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014 is stated as under:



- (i) **Making of Application for Approval:** Every application made to the Central Government under Section 196 shall be in Form No. MR-2 as prescribed by Rule 7 and shall be accompanied by the specified fee. Rule 7 also requires that every such application shall be made to the Central Government within a period of **ninety days from the date of such appointment**.
- (ii) **General Notice to Members:** Before any application is made by a company to the Central Government under section 196, a general notice to the members of the company shall be issued by or on behalf of the company, indicating the nature of the application proposed to be made.
- (iii) **Publication of Notice:** Such notice shall be published:
 - at least once in a newspaper in the principal language of the district in which the registered office of the company is situate and circulating in that district; and
 - at least once in English in an English newspaper circulating in that district.
- (iv) **Attaching of Notice with the Application:** The copies of the notices, together with a certificate by the company as to the due publication thereof, shall be attached to the application.



10. COMPENSATION FOR LOSS OF OFFICE OF MANAGING OR WHOLE-TIME DIRECTOR OR MANAGER [SECTION 202]

Section 202 of the Act contains provisions for compensation for loss of office of Managing Director or Whole-time director or Manager as under:

When payment to be made: A company may make payment to a Managing Director (MD) or Whole-time director (WTD) or Manager	Prohibition on payment of compensation: No payment of compensation shall be made in the following cases-	Quantum of compensation payable to such Managing Director or Whole-time director or manager:

(but not to any other director) by means of:		
• compensation for loss of office, or • as consideration for retirement from office, or • in connection with such loss or retirement.	• where the director resigns from his office as a result of the reconstruction of the company, or of its amalgamation and is appointed as the managing or whole-time director, manager or other officer of the reconstructed company or of the body corporate resulting from the amalgamation; • where the director resigns from his office otherwise than on the reconstruction of the company or its amalgamation <i>i.e.</i> resigns on his own; • where the office of the director is vacated under section 167(1)⁶; • where the company is being wound up, (by an order of the Tribunal or voluntarily), due to the negligence or default of the director; • where the director has been guilty of fraud / breach of trust / of gross negligence / gross mismanagement in relation to the conduct of the affairs of the	shall not exceed the remuneration he would have earned if he would have been in office for the remainder of his term or three years, whichever is shorter. In other words, if the remaining period of his term in the office is more than three years the compensation shall be restricted to three years only; otherwise it is to be paid for the remainder of his term.

⁶ Various grounds of vacation of office covered by Section 167 (1) are mentioned in an earlier Chapter.

	company or any subsidiary company or holding company thereof; and • where the director has instigated/ has taken part directly or indirectly in bringing about, the termination of his office.	

Calculation of compensation: The compensation shall be calculated on the basis of the **average remuneration** earned by him during a period of three years immediately preceding the date on which he ceased to hold such office, or where he held the office of less than three years, then for such shorter period.

No compensation if company is being wound up: No such payment of compensation can be made if winding up of the company is commenced whether:

- before the date on which he has ceased to hold office; or
- within 12 months after the date on which he has ceased to hold office,

if the assets on winding up (after deducting expenses on winding up) are not sufficient to repay the shareholders the share capital, including premiums if any, contributed by them.

Note: Section 202 does not prohibit the payment to a managing director or whole-time director, or manager, of any remuneration for services rendered by him to the company in **any other capacity**.



11. SECRETARIAL AUDIT FOR BIGGER COMPANIES [SECTION 204]

Section 204 of the Act contains provisions for secretarial audit for bigger companies. These provisions are discussed as under:

(i) **Which companies to get conducted secretarial audit:** Section 204(1) requires the following types of companies to get conducted secretarial audit:

- every listed company; and
- a company belonging to the other prescribed class of companies. In this respect Rule 9(1) of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014 prescribes following companies for the purpose of secretarial audit:

(a)	Every public company having a paid-up share capital of 50 crore rupees or more; or

(b)	Every public company having a turnover of 250 crore rupees or more; or
(c)	Every company having outstanding loans or borrowings from banks or public financial institutions of one hundred crore rupees or more.

Explanation to Rule 9 : For the purposes of this sub-rule, it is hereby clarified that the paid up share capital, turnover, or outstanding loans or borrowings as the case may be, existing on the last date of latest audited financial statement shall be taken into account.

- (ii) **Who is authorised to give secretarial audit report:** According to Section 204 (1), a company secretary in practice is authorised to give Secretarial Audit Report. Such Report shall be in Form No.MR - 3⁷.
- (iii) **Annexing of secretarial audit report:** A company shall annex the secretarial audit report so obtained with its Board's report made in terms of section 134 (3).
- (iv) **Duty of the company as regards secretarial audit:** The company is duty-bound to give all assistance and facilities to the company secretary in practice, for auditing the secretarial and related records of the company Section 204(2)].
- (v) **Duty of the Board of Directors:** The Board of Directors, in the Board's Report prepared under section 134(3) shall explain in full any qualification or observation or other remarks made by the company secretary in practice in his report [Section 204 (3)].
- (vi) **Penalty for contravention:** If a company or any officer of the company or the company secretary in practice, contravenes the provisions of Section 204, then

(a)	the company; or
(b)	every officer of the company; or
(c)	the company secretary in practice,

who is in default, shall be liable to a penalty of two lakh rupees [Section 204(4)].

Example 7: Agro Chemical Ltd. a pharmaceutical company wants to know the provision for applicability to conduct secretarial audit. Board of director of the Company appointed an expert to analyse the business of the organisation and advise whether they are contravening the provision of Companies Act, 2013 as they never conducted secretarial audit thinking they don't have enough business transactions to consider these requirements earlier. Company provides you following information: Paid-up share capital rupees 45 crore, Turnover rupees 200 crore and Outstanding

⁷ Form prescribed by Rule 9 (2) of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014.

Loans and Borrowing of rupees 150 crore. In given case, Agro Chemical Ltd. crosses the threshold limit of outstanding loans and borrowings of rupees 100 crore or more for getting Secretarial Audit conducted. Accordingly, Agro chemical Ltd. is required to conduct secretarial audit under Companies Act, 2013.



12. A. PART II OF SCHEDULE V [SECTIONS I TO V] - MANAGERIAL REMUNERATION

B. PART III OF SCHEDULE V-PROVISIONS APPLICABLE TO PARTS I AND II

C. PART IV OF SCHEDULE V-EXEMPTION BY CENTRAL GOVERNMENT

A. PART II OF SCHEDULE V [SECTIONS I TO V] – Managerial Remuneration

(i) **SECTION I - Remuneration payable by companies having profits:** Subject to the provisions of Section 197, a company having profits in a financial year may pay remuneration to a managerial person or persons or other director or directors not exceeding the limits specified in such section.

Note: Refer Provisions of Section 197 discussed earlier.

(ii) **SECTION II - Remuneration payable by companies having no profit or inadequate profit [Discussed earlier u/s Section 197(3)]**

(iii) **SECTION III — Remuneration payable by companies having no profit or inadequate profit in certain special circumstances:** In the following circumstances a company may pay remuneration to a managerial person or other director in excess of the amounts provided in Section II above:

- (a) where the remuneration in excess of the limits specified in Section I or II is paid by any other company and that other company is either a foreign company or has got the approval of its shareholders in general meeting to make such payment, and treats this amount as managerial remuneration for the purpose of section 197 and the total managerial remuneration payable by such other company to its managerial persons or other directors including such amount or amounts is within permissible limits under section 197.

(b) where the company—

(i)	a newly incorporated company	for a period of seven years from the date of its incorporation, or	it may pay any remuneration to its managerial persons or other directors
(ii)	is a sick company , for whom a scheme of revival or rehabilitation has been ordered by the Board for Industrial and Financial Reconstruction	for a period of five years from the date of sanction of scheme of revival, or	
(iii)	is a company in relation to which a resolution plan has been approved by the National Company Law Tribunal under the Insolvency and Bankruptcy Code, 2016	for a period of five years from the date of such approval,	

(c) where remuneration of a managerial person or other director exceeds the limits in Section II but the remuneration has been fixed by the Board for Industrial and Financial Reconstruction or the National Company Law Tribunal:

Provided that the limits under this Section shall be applicable subject to meeting all the conditions specified under Section II and the following additional conditions:

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

Explanation- For the purposes of Section I, Section II, and Section III, the term “ or other director” shall mean a non-executive director or an independent director.

(iv) SECTION IV— Perquisites not included in managerial remuneration:

1. A managerial person shall be eligible for the following perquisites which shall not be included in the computation of the ceiling on remuneration specified in Section II and

Section III:

- (a) **Contribution to provident fund, superannuation fund or annuity fund** to the extent these either singly or put together are not taxable under the Income-tax Act, 1961;
 - (b) **Gratuity** payable at a rate not exceeding half a month's salary for each completed year of service; and
 - (c) **Encashment of leave** at the end of the tenure.
2. In addition to the perquisites specified in paragraph 1 of this section, an expatriate managerial person (including a non-resident Indian) shall be eligible to the following perquisites which shall not be included in the computation of the ceiling on remuneration specified in Section II or Section III:
- (a) **Children's education allowance:** In case of children studying in or outside India, an allowance limited to a maximum of rupees 12,000 per month per child or actual expenses incurred, whichever is less. Such allowance is admissible up to a maximum of two children.
 - (b) **Holiday passage for children studying outside India or family staying abroad:** Return holiday passage once in a year by economy class or once in two years by first class to children and to the members of the family from the place of their study or stay abroad to India if they are not residing in India, with the managerial person.
 - (c) **Leave travel concession:** Return passage for self and family in accordance with the rules specified by the company where it is proposed that the leave be spent in home country instead of anywhere in India.

Explanation I.— For the purposes of this Schedule, “family” means the spouse, dependent children and dependent parents of the managerial person.

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

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

Explanation III — For the purposes of this Schedule, “**negative effective capital**” means the effective capital which is calculated in accordance with the provisions contained in Explanation I of this Part is less than zero.

Explanation IV — For the purposes of this Schedule: —

- (A) *Omitted*
- (B) “Remuneration” means remuneration as defined in clause (78) of Section 2 and includes reimbursement of any direct taxes to the managerial person.

(v) SECTION V—Remuneration payable to a managerial person in two companies:

Subject to the provisions of sections I to IV, a managerial person shall draw remuneration from one or both companies, provided that the total remuneration drawn from the companies does not exceed the higher maximum limit admissible from any one of the companies of which he is a managerial person.

B. PART III OF SCHEDULE V- Provisions applicable to Parts I and II

1. The appointment and remuneration referred to in Part I and Part II of this Schedule shall be subject to approval by a resolution of the shareholders in general meeting.
2. The auditor or the Secretary of the company or where the company is not required to appoint a Secretary, a Secretary in whole-time practice shall certify that the requirement of this Schedule have been complied with and such certificate shall be incorporated in the return filed with the Registrar under sub-section (4) of section 196.

C. PART IV OF SCHEDULE V: Exemption by Central Government

The Central Government may, by notification, exempt any class or classes of companies from any of the requirements contained in this Schedule.

Clarification

The MCA vide General Circular No. 07/2015 dated 10th April, 2015 has clarified that a managerial person who has been appointed in accordance with provisions of Schedule XIII of the Companies Act, 1956, may continue to receive remuneration for his remaining term in accordance with terms and conditions approved by the company as per relevant provisions of Schedule XIII of the Companies Act, 1956 even if the part of his/her tenure falls after 1st April, 2014.

TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. *Due to non-compliance of certain requirements under the Companies Act, 2013 not amounting to fraud, Shikha Super-Market Limited was required to re-state its financial statements for the financial year 201718 during the current year. After the financial statements were restated, it was found that Mr. Kumar, the Managing Director (MD) of that period, who is now retired, was paid excess remuneration to the extent of ₹ 5,00,000. In the given situation, choose the correct option out of those given below, which indicates whether such excess remuneration paid to ex-MD Mr. Kumar is recoverable or not.*
 - (a) *Excess remuneration of ₹ 5,00,000 paid to Mr. Kumar, ex-MD of Shikha Super-Market Limited, cannot be recovered since such recovery after retirement is invalid.*
 - (b) *Excess remuneration of ₹ 5,00,000 paid to Mr. Kumar, ex-MD of Shikha Super-Market Limited, shall be recovered irrespective of his retirement from the company.*
 - (c) *Only ₹ 2,50,000, being 50% of excess remuneration of ₹ 5,00,000, paid to Mr. Kumar, ex-MD of Shikha Super-Market Limited, is validly recoverable because no fraud implicating him is involved.*
 - (d) *Only ₹ 1,25,000, being 25% of excess remuneration of ₹ 5,00,000, paid to Mr. Kumar, ex-MD of Shikha Super-Market Limited, is validly recoverable because no fraud implicating him is involved.*

2. *The Board of Directors of Capable Hospitality Services Limited has entrusted Mr. Vikas, the newly appointed Managing Director (MD) of the company, with some powers. However, Mr. Vikas is not interested in discharging administrative functions as authorised by the Board of Directors, since he is of the view that he should have been entrusted with substantial powers of the management. Out of the following four options, which one is correctly applicable in relation to the functions which Mr. Vikas, the MD of Capable Hospitality Services Limited, can undertake:*
 - (a) *To draw and endorse any cheque on the account of Capable Hospitality Services Limited maintained with National Commercial Bank Limited, the main banker of the company.*
 - (b) *To sign the financial statements of Capable Hospitality Services Limited.*
 - (c) *To draw and endorse any bill of exchange when it exceeds ₹ 1,00,000.*
 - (d) *To draw and endorse any bill of exchange when it exceeds ₹ 5,00,000.*

3. *Mr. Joseph Daniel, holding the office of Whole-time Director (WTD) in Tasty Choco-Chips Limited, is desirous of appointing Mr. Vanilla Sequera, who has attained the age of 72 years, as the Managing Director (MD) of the company. However, the Board of Directors is of the opinion that no company shall appoint or continue the employment of any person as Managing Director,*

Whole-time Director or Manager who is below the age of twenty-one years or has attained the age of seventy years. From the following four options, select the one which is applicable in relation to the validity or invalidity of appointing Mr. Vanilla Sequera as the Managing Director (MD) of Tasty Choco-Chips Limited:

- (a) In spite of the fact that Mr. Vanilla Sequera has attained the age of 72 years, he can be validly appointed as Managing Director by the Board of Directors of Tasty Choco-Chips Limited when the recommendation has been made by Mr. Joseph Daniel, the Whole-time Director.
 - (b) Since Mr. Vanilla Sequera has attained the age of 72 years, he cannot be validly appointed as Managing Director of Tasty Choco-Chips Limited.
 - (c) In spite of the fact that Mr. Vanilla Sequera has attained the age of 72 years, he can be validly appointed as Managing Director by the shareholders of Tasty Choco-Chips Limited through passing a Special Resolution in general meeting.
 - (d) In spite of the fact that Mr. Vanilla Sequera has attained the age of 72 years, he can be validly appointed as Managing Director of Tasty Choco-Chips Limited if an application is made to the jurisdictional National Company Law Tribunal (NCLT) and its permission is received for such appointment.
4. On June, 20, 2019, Mr. Anil Mehra was appointed as Manager of PQR Music Systems Limited for a period of five years. Considering his performance and dedication towards the company, the management of PQR Music Systems Limited decided to re-appoint him as Manager before the completion of his tenure. Out of the following four options, choose the one which indicates the date on which his re-appointment will be considered valid?
- (a) June 24, 2023
 - (b) February 1, 2023
 - (c) March 12, 2022
 - (d) September 10, 2022
5. Lockworth Safety Gears Limited which pays remuneration to its Directors on yearly basis, has Harsha as Whole-time Director (WTD). Recently, the company appointed Mr. Raviyansh as Managing Director (MD). While paying remuneration, Lockworth Safety Gears Limited needs to keep in view that the overall remuneration payable to the Directors including Managing Director, Whole-time Director and Manager shall not exceed maximum limit prescribed under the relevant provisions. After the appointment of Mr. Raviyansh as Managing Director, since the company has both Whole-time Director as well as Managing Director, select the appropriate option from those given below which indicates the maximum remuneration that is allowed in a Financial Year:
- (a) 3% of net profits.
 - (b) 5% of net profits.

- (c) 10% of net profits.
- (d) 11% of net profits.
6. Mr. Abhishek has been in full time employment at F&I Limited (a listed company) working as Chief Financial Officer (CFO). He has been given the offer to hold the office of Whole-time Director at M&N Limited whose more than 51% of the paid-up share capital is held by F&I Limited. After considering the applicable provisions, you are required to choose the correct option from the following four which indicates whether Mr. Abhishek can validly proceed or not with the offer of Whole-time Director extended by M&N Limited while also continuing as Chief Financial Officer (CFO) of F&I Limited:
- (a) Mr. Abhishek can validly proceed with the offer of Whole-time Director at M&N Limited while also continuing as Chief Financial Officer (CFO) because being a Key Managerial Personnel he shall not be disentitled from accepting the offer of Whole-time Director in any other company after obtaining the permission of Board of Directors of his parent company i.e., F&I Limited.
- (b) Mr. Abhishek will not be able to proceed with the offer of Whole-time Director at M&N Limited since a whole time Key Managerial Personnel cannot hold office in more than one company at the same time.
- (c) Mr. Abhishek can proceed with the offer of Whole-time Director at M&N Limited while also continuing as Chief Financial Officer (CFO) since M&N Limited is a subsidiary of F&I Limited.
- (d) Mr. Abhishek will not be able to proceed with the offer of Whole-time Director at M&N Limited since a whole time Key Managerial Personnel cannot hold office in more than one company at the same time including its subsidiary company.
7. Hasmukh Entertainment Limited, incorporated under the Companies Act, 2013, appointed Mr. Ram Kishore, a well-qualified and experienced person, as Whole-time Director (WTD) for a period of five years in the Annual General Meeting (AGM) held on August 28, 2019. In order that Mr. Ram Kishore continues with the company as Wholetime Director (WTD), he was re-appointed in advance as Whole-time Director (WTD) for another term of five years in the Annual General Meeting which was held on September 28, 2021. The second term of five years will start after the expiry of first term in August, 2024. From the following alternatives, choose the one which indicates the validity or otherwise of re-appointment of Mr. Ram Kishore for the second term of five years by the company:
- (a) The re-appointment of Mr. Ram Kishore in advance as Wholetime Director (WTD) for another term of five years is valid because re-appointment can be made for a period not exceeding 5 years at any time provided the Articles of Association of the company provide for such re-appointment before one year from the completion of his 'yet-to-expire' term.

- (b) *The re-appointment of Mr. Ram Kishore in advance as Wholetime Director (WTD) for another term of five years is invalid because his re-appointment as Whole-time Director (WTD) cannot be made earlier than one year before the expiry of his first term.*
- (c) *The re-appointment of Mr. Ram Kishore in advance as Wholetime Director (WTD) for another term of five years is valid provided the resolution for such re-appointment had earlier been passed with the consent of all the Directors present at the Board Meeting and thereafter, such re-appointment was taken up at the Annual General Meeting for approval.*
- (d) *The re-appointment of Mr. Ram Kishore in advance as Wholetime Director (WTD) for another term of five years is invalid because no special resolution for his re-appointment was passed at the Annual General Meeting for approval.*

Descriptive Questions

1. *Advise Super Specialities Ltd. in respect of the following proposals under consideration of its Board of Directors:*
 - (i) *Payment of commission of 4% of the net profits per annum to the directors of the company;*
 - (ii) *Payment of remuneration of rupees 40,000 per month to the whole-time director of the company which is running in loss and having an effective capital of rupees 95 lacs.*
2. *Mr. X, a Director of MJV Ltd., was appointed as Managing Director on 1st April 2017. One of the terms of appointment was that in the absence of adequacy of profits or if the company had no profits in a particular year, he will be paid remuneration in accordance with Schedule V. For the financial year ended 31st March 2019, the company suffered heavy losses. The company was not in a position to pay any remuneration but he was paid 50 lakhs for the year. The effective capital of the company is 150 crores. Referring to the provisions of the Companies Act, 2013, as contained in Schedule V, examine the validity of the above payment of remuneration to Mr. X.*
3. *Mr. Doubtful was appointed as Managing Director of Carefree Industries Ltd. for a period of five years with effect from 1.4.2016 on a salary of 12 lakhs per annum with other perquisites. The Board of Directors of the company came to know about certain questionable transactions entered into by Mr. Doubtful and therefore, terminated his services as Managing Director from 1.3.2019. Mr. Doubtful termed his removal as illegal and claimed compensation from the company. Meanwhile the company paid a sum of ₹ 5 lakhs on adhoc basis to Mr. Doubtful pending settlement of his dues. Discuss whether:*
 - (i) *The company is bound to pay compensation to Mr. Doubtful and, if so, how much.*
 - (ii) *The company can recover the amount of 5 lakhs paid on the ground that Mr. Doubtful is not entitled to any compensation, because he is guided by corrupt practices.*

4. International Technologies Limited, a listed company, being managed by a Managing Director proposes to pay the following managerial remuneration:

- (i) Commission at the rate of five percent of the net profits to its Managing Director, Mr. Kamal.
- (ii) The directors other than the Managing Director are proposed to be paid monthly remuneration of rupees 50,000 and also commission at the rate of one percent of net profits of the company subject to the condition that overall remuneration payable to ordinary directors including monthly remuneration payable to each of them shall not exceed two percent of the net profits of the company. The commission is to be distributed equally among all the directors.
- (iii) The company also proposes to pay suitable additional remuneration to Mr. Bhatt, a director, for professional services rendered as software engineer, whenever such services are utilized.

You are required to examine with reference to the provisions of the Companies Act, 2013 the validity of the above proposals.

5. The following particulars are extracted from the statement of profit and loss of Surya Cement Limited for the year ended 31st March 2023:

Sr. No	Particulars	Amount
1)	Gross Profit	60,00,000
2)	Profit on sale of building (Cost ₹ 10,00,000 and written down value ₹ 6,00,000)	5,00,000
3)	Salaries & wages	2,50,000
4)	Sundry Repairs to Fixed Assets	1,00,000
5)	Subsidy from the government	3,00,000
6)	Compensation for breach of contract	1,00,000
7)	Depreciation	1,40,000
8)	Loss on sale of investments	2,00,000
9)	Interest on unsecured loans	50,000
10)	Interest on debentures issued by the company	1,00,000
11)	Repair Expenses to fixed assets (Capital in nature)	2,00,000
12)	Net Profit	13,00,000

You are required to calculate the overall managerial remuneration payable under section 197 of the Companies Act, 2013 subject to the provisions under Schedule V.

6. You are provided with the relevant extract of the financials of Tribhuke Limited for the financial year ended as on 31st March 2023 as below:

Sr. No	Particulars	Amount
1	Authorised Share Capital	10,00,00,00,000
2	Issued and Paid up Share Capital	5,00,00,000
3	Share Premium Account	25,00,000
4	Reserves and Surplus (Amount of ₹ 25,00,000 is included as Revaluation Reserve)	35,00,000
5	Term loan repayable after 1 year	12,00,000
6	Current Borrowings (Cash Credit Loan from Banks)	20,00,000
7	Non-Current Investments	10,00,000
8	Accumulated Losses	5,00,000
9	Preliminary expenses not written off	3,00,000

The company has three managerial persons in its Board of Directors – Mr. A – Managing Director, Mr. B – Whole Time Director and Mr. C – Director-. According to their terms of appointment, in case the company has no or inadequate profits, the managerial remuneration payable to them shall be in accordance with Schedule V. You are required to compute the total managerial remuneration payable considering the provisions of Schedule V.

ANSWERS

Answer to Multiple Choice Questions

1.	b	2.	b	3.	c	4.	a	5.	c
6.	c	7.	b						

Answer to Descriptive Questions

- Under section 197 (1) the limit of total managerial remuneration payable by a public company, to its directors, including managing director and whole-time director, and its manager in respect of any financial year shall not exceed eleven per cent of the net profits of that company for that financial year computed in the manner laid down in section 198. Further, the third proviso to section 197 (1) provides that except with the approval of the company in general meeting by a special resolution, the remuneration payable to directors who are neither managing directors nor whole-time directors shall not exceed one per cent. of the net profits of the company, if there is a managing or whole-time director or manager. Whereas in any other case, the remuneration payable to directors shall not exceed three per cent of the net profits.

Therefore, in the given case, the commission of 4% is beyond the limit specified, and the same should be approved by the members by passing a special resolution.

- (ii) As per section 197(3) of the Companies Act, 2013, if, in any financial year, a company has no profits or its profits are inadequate, the company shall not pay to its directors, including managing or whole time director or manager or any other non-executive director, including an independent director, any remuneration exclusive of any fees payable to directors except in accordance with the provisions of Schedule V. Section II of Part II of Schedule V provides that where in any financial year during the currency of tenure of a managerial person or other director, a company has no profits or its profits are inadequate, it may pay remuneration to the managerial person not exceeding 60 lakhs for the year if the effective capital of the company is negative or upto 5 crore.

In the given situation, the proposed remuneration of 40,000 rupees per month (*i.e.* 4,80,000 rupees per annum) can be paid to the whole-time director of the company which is running in loss because the remuneration is within the permissible limit of 60 lakhs.

2. Under Section II of Part II of Schedule V to the Companies Act, 2013, the remuneration payable to managerial personnel is linked to the effective capital of the company. Schedule V states that where in any financial year during the currency of tenure of a managerial person or other director, a company has no profits or its profits are inadequate, it may pay remuneration to the managerial person not exceeding 120 Lakhs in the year in case the effective capital of the company is between 100 crores and 250 crores. However, the remuneration in excess of 120 Lakh may be paid if the resolution passed by the shareholders is a special resolution.

From the foregoing provisions as contained in Schedule V, the payment of 50 lakh in the year of loss as remuneration to Mr. X is less than 120 lakhs which is otherwise permissible when the effective capital of the company is between 100 crores and 250 crores. Thus, payment of 50 lakhs being made to Mr. X is within the prescribed limit and can be validly made to him.

3. According to Section 202 of the Companies Act, 2013, compensation can be paid only to a Managing Director, Whole-time Director or Manager. The amount of compensation cannot exceed the remuneration which he would have earned if he would have been in the office for the unexpired term of his office or for 3 years whichever is shorter. No compensation shall be paid, if the director has been found guilty of fraud or breach of trust or gross negligence in the conduct of the affairs of the company.

In light of the above provisions of law, the company is not liable to pay any compensation to Mr. Doubtful, if he has been found guilty of fraud or breach of trust or gross negligence in the conduct of affairs of the company. But it is not proper on the part of the company to withhold the payment of compensation on the basis of mere allegations. The compensation payable by the company to Mr. Doubtful would be 25 Lakhs calculated at the rate of 12 Lakhs per annum for unexpired term of 25 months.

Regarding *ad-hoc* payment of 5 Lakhs, it will not be possible for the company to recover the amount from Mr. Doubtful in view of the decision in case of *Bell vs. Lever Bros. (1932) AC 161* where it was observed that a director was not legally bound to disclose any breach of his fiduciary obligations so as to give the company an opportunity to dismiss him. In that case the Managing Director was initially removed by paying him compensation and later on it was discovered that he had been guilty of breaches of duty and corrupt practices and that he could have been removed without compensation.

4. International Technologies Limited, a listed company, being managed by a Managing Director proposes to pay the following managerial remuneration:

- (i) **Commission at the rate of 5% of the net profits to its Managing Director, Mr. Kamal:** Part (i) of the Second Proviso to Section 197(1), provides that except with the approval of the company in general meeting by a special resolution, the remuneration payable to any one managing director or whole time director or manager shall not exceed 5% of the net profits of the company and if there is more than one such director then remuneration shall not exceed 10% of the net profits to all such directors and manager taken together.

In the present case, since the International Technologies Limited is being managed by a Managing Director, the commission at the rate of 5% of the net profit to Mr. Kamal, the Managing Director is allowed and no approval of company in general meeting is required.

- (ii) The directors other than the Managing Director are proposed to be paid monthly remuneration of rupees 50,000 and also commission at the rate of 1 % of net profits of the company subject to the condition that overall remuneration payable to ordinary directors including monthly remuneration payable to each of them shall not exceed 2 % of the net profits of the company: Part (ii) of the Second Proviso to Section 197(1) provides that except with the approval of the company in general meeting by a special resolution, the remuneration payable to directors who are neither managing directors nor whole time directors shall not exceed-

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

In the present case, the maximum remuneration allowed to directors other than managing or whole-time director is 1% of the net profits of the company because the company is managed by a managing director. Hence, if the company wants to fix directors' remuneration at not more than 2% of the net profits of the company, the approval of the company in general meeting is required by passing a special resolution.

(iii) The company also proposes to pay suitable additional remuneration to Mr. Bhatt, a director, for professional services to be rendered by him as software engineer, whenever such services are utilized by the company:

(1) According to section 197(4), the remuneration payable to the directors of a company, including any managing or whole-time director or manager, shall be determined, in accordance with and subject to the provisions of this section, either

(i) by the articles of the company, or

(ii) by a resolution or,

(iii) if the articles so require, by a special resolution, passed by the company in general meeting, and

(2) the remuneration payable to a director determined aforesaid shall be inclusive of the remuneration payable to him for the services rendered by him in any other capacity.

(3) Any remuneration for services rendered by any such director in other capacity shall not be so included if—

(i) the services rendered are of a professional nature; and

(ii) in the opinion of the Nomination and Remuneration Committee, if the company is covered under sub-section (1) of section 178, or the Board of Directors in other cases, the director possesses the requisite qualification for the practice of the profession.

Hence, in the present case, the additional remuneration payable to Mr. Bhatt, a director, for professional services rendered by him as software engineer will not be included in the maximum managerial remuneration. Accordingly, such additional remuneration shall be allowed but opinion of Nomination and Remuneration Committee needs to be obtained.

Also, the International Technologies Limited (a listed company) shall disclose in the Board's report, the ratio of the remuneration of each director to the median employee's remuneration and such other details as are prescribed under Rule 5 of the Companies (Appointment and Remuneration of Managerial personnel) Rules, 2014.

5. The managerial remuneration shall be computed in accordance with the provisions laid down in section 198 of the Companies Act 2013

Particulars	Amount
Net profit	13,00,000
Less: Capital profits on sale of building (Note 1)	1,00,000
Salaries & Wages (Note 2)	-
Sundry repairs to fixed Assets (Note 2)	-
Subsidy from the government (Note 3)	-
Compensation from breach of contract (Note 2)	-
Depreciation (Note 2)	-
Loss on Sale of Investments (Note 4)	-
Interest on unsecured loans (Note 2)	-
Interest on debentures (Note 2)	-
Add: Repair expenses to fixed assets (Capital in Nature) (Note 5)	2,00,000
Net profits as per section 198	14,00,000

Therefore, the overall maximum managerial remuneration shall be 11% of the Net profits computed in accordance with section 198 i.e. $11\% \times 14,00,000 = ₹ 1,54,000$. It is assumed that the net profit given in the question is arrived after giving effect to all the line items given therein.

Notes:

- As per section 198(3), credit shall not be given for profits from the sale of any immovable property or fixed assets of a capital nature comprised in the undertaking or any of the undertakings of the company, unless the business of the company consists, whether wholly or partly, of buying and selling any such property or assets; provided that where the amount for which any fixed asset is sold exceeds the written-down value thereof, credit shall be given for so much of the excess as is not higher than the difference between the original cost of that fixed asset and its written-down value.

Accordingly, the calculation of capital profit is computed as under:

Profit = Selling Price – Written down value

5,00,000 = Selling Price – 6,00,000. Therefore, Selling Price = 11,00,000. Capital profit = 11,00,000 – 10,00,000 (original cost) = 1,00,000

- 2) According to section 198 (4), the following sums shall be deducted:
- All the usual working charges – salaries and wages are considered as usual working charges
 - expenses on repairs, whether to immovable or to movable property, provided the repairs are not of a capital nature
 - any compensation or damages to be paid in virtue of any legal liability including a liability arising from a breach of contract
 - interest on debentures issued by the company
 - interest on unsecured loans and advances
 - depreciation to the extent specified in section 123

Since all of the above charges are already deducted while arriving at net profit, no effect will be given.

- 3) According to section 198 (1), credit shall be given for bounties and subsidies received from any government, or any public authority constituted or authorised in this behalf, by any government, unless and except in so far as the Central Government otherwise directs.
- 4) According to section 198(5), Loss of a capital nature including loss on sale of the undertaking or any of the undertakings of the company or any part thereof shall not be deducted. In the given question, in the absence of the specific information about the nature of investments, the said investments are considered as current investments and revenue in nature and accordingly no effect is given as it is already deducted while arriving at net profit.
- 5) According to section 198(4), expenses on repairs, whether to immovable or to movable property is deducted only for repairs which are not capital in nature. Accordingly, we have added back to the net profit.
6. Section II of Part II of Schedule V states the provisions applicable for the payment of managerial remuneration in case where the company has no profits or its profits are inadequate. In such a case, managerial remuneration is payable on the basis of the effective capital as on the last date of the financial year for which the remuneration is payable. Accordingly, to compute the total managerial remuneration payable, effective capital is calculated as:

Particulars	Amount
Issued and Paid up Capital	5,00,00,000
Add: Share Premium Account	25,00,000

Add: Reserves and surplus excluding revaluation reserve	10,00,000
Add: Term Loan repayable after 1 year (excluding working capital loans)	12,00,000
Less: Non-Current Investments	10,00,000
Less: Accumulated Losses	5,00,000
Less: Preliminary Expenses	3,00,000
Effective Capital	5,29,00,000

Explanation 1 to Section II of Part II of Schedule V states effective capital means the aggregate of the paid-up share capital (excluding share application money or advances against shares); amount, if any, for the time being standing to the credit of share premium account; reserves and surplus (excluding revaluation reserve); long-term loans and deposits repayable after one year (excluding working capital loans, over drafts, interest due on loans unless funded, bank guarantee, etc., and other short-term arrangements) as reduced by the aggregate of any investments (except in case of investment by an investment company whose principal business is acquisition of shares, stock, debentures or other securities), accumulated losses and preliminary expenses not written off.

Section II of Part II of Schedule V states that where the effective capital is 5 crores and above but less than 100 crores, the remuneration payable shall not exceed Rs. 84 lakhs. Accordingly, the total managerial remuneration payable by the Companies to three managerial personnel for the year ended 31st March, 2023 shall not exceed ₹ 252 lakhs (₹ 84 lakhs x 3 managerial personnel).

Note: As nothing is specified about Mr. C, whether he is part-time or non-executive or Independent director, he may be considered as director in whole time employment.

[illegible]

CHAPTER

3

MEETINGS OF BOARD AND ITS POWERS



LEARNING OUTCOMES

At the end of this Chapter, you will be able to:

- ❑ Elaborate the procedure and requirements of convening a Board meeting.
- ❑ Explain about the requisite quorum for the conduct of Board meetings.
- ❑ Recognise the concept of Audit Committee, Nomination and Remuneration Committee, and Stake-holders Relationship Committee of the Board.
- ❑ Explain the powers and restrictions imposed on the powers of Board.
- ❑ Describe the various provisions relating to contributions to be made by companies to charitable funds, political parties, National Defence Fund, etc.
- ❑ Comprehend the provisions relating to disclosure of interest by directors, restrictions on loan to directors and loans and investments made by a company.
- ❑ Explain the provision of related party and the related party transactions.
- ❑ Determine the provisions related to the payment to directors for loss of office, etc. in connection with transfer of undertaking, property or shares.



1. INTRODUCTION

The shareholders in general meetings and the directors acting collectively as a Board conduct the affairs of a company. Therefore, directors frequently meet to discuss various matters relating to the management and administration of the affairs of the company in the interest of the shareholders, the company and the public at large including society and economy and more particularly, the environment. The modern practice is to confer upon the directors the right to exercise all powers of the company in which they are appointed as directors except for those matters, which by law are required to be exercised by the company in general meetings through the shareholders. The Board of directors oversees management of the company to ensure that the interests of the shareholders are protected and the goal of wealth maximization is achieved.

The provisions related to meetings of Board and its powers are dealt with under Sections 173 to 193 of the Companies Act, 2013 (in short, the 'Act') and the relevant Rules.



2. MEETINGS OF BOARD [SECTION 173]

Section 173 of the Act contains provisions which deal with Meetings of the Board. This section requires the directors upon whose shoulders the management of the company rests to meet and interact regularly. The aim is to ensure that the powers which vest in the directors should be exercised collectively and every director should have the knowledge of the decisions taken for the smooth conduct of the business operations. The provisions of Section 173 are discussed hereunder:

(i) Frequency of Board Meetings [Section 173 (1)]¹:

- (a) **First Board meeting:** Every company shall hold the first meeting of the Board of Directors **within 30 days** of the date of its Incorporation.
- (b) **Subsequent Board meetings:** Every company shall hold minimum of 4 meetings every year but the gap between two consecutive board meetings shall not be **more than 120 days**.

Example 1: In case a company conducted its Board meeting on 2nd April, 2019, then the next meeting must be held within 120 days of this date *i.e.* ideally before 31st July, 2019; and, by 31st December, 2019, the company must conduct minimum four such meetings (including the meetings which have already been conducted in the year 2019). The Board meetings may go beyond four also in a calendar year depending upon the urgency of any business.

¹ As per Para 2.1 of Revised Secretarial Standards-1 (SS-1), the company shall hold at least four Meetings of its Board in each Calendar Year with a maximum interval of one hundred and twenty days between any two consecutive Meetings.

(ii) **Exemptions to Certain Companies [Section 173(5)]:**

In case of a **One Person Company (OPC)**, **small company** and **dormant company**, the provision regarding conducting of **four** Board meetings every year is **not applicable**. These entities are required to conduct **one Board meeting in each half of a calendar year** and the gap between the two meetings must **not be less than 90 days**. This is the minimum requirement and if so done, they shall be deemed to have complied with the provisions of Section 173.

OPC having only one director: One more exemption is given to One Person Company which has only one director on its Board of Directors. Such OPC shall not be required to hold even a single Board meeting during the year. Thus, it is totally exempted from the provisions of Section 173(5)².

Modifications in respect of Section 8 companies and Private companies

1. Vide Notification No. G.S.R.466(E) dated 5th June, 2015 as amended by Notification No. G.S.R. 584 (E) dated 13th June, 2017, Section 173 (1) shall apply to a **Section 8 company** only to the extent that the Board of Directors of such a company shall hold **at least one meeting within every six calendar months**. This is subject to the conditions that the company has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar.

2. Vide Notification No. GSR 464(E), dated 5-6-2015, as amended by Notification No. GSR 583(E), dated 13-6-2017, in case of **private companies**, for sub-section (5) of Section 173, the following sub-section shall be substituted:

"(5) A One Person Company, small company, dormant company and a private company (if such private company is a start-up) shall be deemed to have complied with the provisions of this section if at least one meeting of the Board of Directors has been conducted in each half of a calendar year and the gap between the two meetings is not less than ninety days:

Provided that nothing contained in this sub-section and in section 174 shall apply to One Person Company in which there is only one director on its Board of Directors."

The above substitution is effective subject to the conditions that the private company has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar.

² Refer Proviso to Section 173 (5).

(iii) **Participation by Directors in Board Meetings:**

- (a) **Means to attend Board Meetings:** Section 173(2) of the Act allows the directors of a company to attend Board meetings in the following manner:



- in person
- through video conferencing
- other audio-visual means as prescribed under Rule 3 of the Companies (Meetings of Board and its Powers) Rules, 2014

Thus, the directors besides meeting in person, are also permitted to meet through electronic mode *i.e.* video conferencing or other prescribed audio-visual means.

Meaning of the term “video conferencing or other audio-visual means”: It refers to audio-visual electronic communication facility employed which enables all the persons participating in a meeting to communicate concurrently with each other without an intermediary and to participate effectively in the meeting. **[as per Explanation to Rule 3]**

Essentials of audio-visual means: According to Section 173 (2), the audio-visual means should be capable of-

- recording and recognising the participation of the directors; and
- recording and storing the proceedings of such meetings along with date and time.

Matters which cannot be dealt with in a meeting through electronic mode³: The Central Government may, by notification, specify matters which shall not be dealt with in a meeting through video conferencing and other audio-visual means.

Provided further that where there is quorum in a meeting through physical presence of directors, any other director may participate through video conferencing or other audio visual means in such meeting on any matter specified under the first proviso.

- (b) **Procedural points relating to meetings of Board that are held through video conferencing or other audio-visual means:** The procedural points as given in Rule 3 of the Companies (Meetings of Board and its Powers) Rules, 2014, are as under:

³ As per First Proviso to Section 173 (2).

Sl. No.	Procedural aspects relating to meetings of Board that are held through video conferencing or other audio-visual means	For convening and conducting of the Board meetings
1.	Every Company shall make necessary arrangements	to avoid failure of video or audio-visual connection
2.	The Chairperson of the meeting and the company secretary, if any, shall take due and reasonable care-	(A) to safeguard the integrity of the meeting by ensuring sufficient security and identification procedures; (B) to ensure availability of proper video conferencing or other audio-visual equipment or facilities for providing transmission of the communications for effective participation of the directors and other authorized participants at the Board meeting; (C) to record proceedings and prepare the minutes of the meeting; (D) to store for safekeeping and marking the tape recording(s) or other electronic recording mechanism as part of the records of the company at least before the time of completion of audit of that particular year. (E) to ensure that no person other than the concerned director is attending or have access to the proceedings of the meeting through video conferencing mode or other audio-visual means; (F) to ensure that participants attending the meeting through audio visual means are able to hear and see the other participants clearly during the course of the meeting;

3.	Notice of the meeting and the further process	(A) Notices shall be sent to all the directors as per Section 173 (3); (B) Notices shall inform the directors regarding the options available to them to participate through video conferencing mode or other audio-visual means, along with all the necessary information to enable the directors to participate through such mode; (C) A director intending to participate through video conferencing mode or other audio-visual means shall communicate his intention to the Chairperson or the company secretary of the company; (D) If a director intends to participate through video conferencing or other audio-visual means, he shall give prior intimation to that effect, to enable the company to make suitable arrangements in this behalf; (E) Any director who intends to participate in the meeting through electronic mode may intimate about such participation at the beginning of the calendar year and such declaration shall be valid for one year; However, such declaration shall not debar him from participation in the meeting in person in which case he shall intimate the company sufficiently in advance of his intention to participate in person; (F) In the absence of any such intimation (<i>i.e.</i> participation through video conferencing mode or other audio-visual means) from the director, it shall be assumed that he will attend the meeting in person.
4.	Process of roll call at the Board Meeting	At the commencement of the meeting, a roll call shall be taken by the Chairperson. At this point, every director participating through video

		conferencing or other audio-visual means shall state, for the record, the following namely: (a) name; (b) the location from where he is participating; (c) received the agenda and all the relevant material for the meeting; and (d) no one other than the concerned director is attending /having access to the proceedings of the meeting at the location mentioned in clause (b);
5.	After the roll call	The Chairperson or the Company Secretary shall inform the Board about the names of persons other than the directors who are present for the said meeting with the permission of the Chairperson and confirm that the required quorum is complete.
6.	Counting for quorum and ensuring of quorum	A director participating in a meeting through video conferencing or other audio-visual means shall be counted for the purpose of quorum. He shall not be counted if he is to be excluded for any items of business under any provisions of the Act or the rules. The Chairperson shall ensure that the required quorum is present throughout the meeting.
7.	Scheduled venue of the meeting as mentioned in the notice convening the meeting	Scheduled venue shall be deemed to be the venue of the meeting which is conducted through video conferencing or other audio-visual means authorized under these rules and all recordings at such meeting shall be deemed to have been made at that place.
8.	Signing of Statutory Registers placed at the scheduled venue of the	The statutory registers shall be deemed to have been signed by the directors participating through electronic mode, if they have given their

	meeting	consent to this effect and it is so recorded in the minutes of the meeting.
9.	Identification of participant	Every participant shall identify himself for the record before speaking on any item of business on the agenda.
10.	Statement interrupted or garbled	If a statement of a director in the meeting through video conferencing or other audio-visual means is interrupted or garbled, the Chairperson or Company Secretary shall request for a repeat or reiteration.
11.	Objection against a motion	If a motion is objected to and there is a need to put it to vote, the Chairperson shall call the roll and note the vote of each director who shall identify himself while casting his vote.
12.	No access to unauthorized person	From the commencement of the meeting till its conclusion, no person except the Chairperson, Directors, Company Secretary and any other person whose presence is required by the Board shall be allowed access to the place where any director is attending the meeting either physically or through video conferencing without the permission of the Board.
13.	Summary of decision on each agenda item	At the end of discussion on each agenda item, the Chairperson of the meeting shall announce the summary of the decision taken on such item along with names of the directors, if any, who dissented from the decision taken by majority.
14.	Preservation of draft minutes	Draft minutes shall be preserved till their confirmation. Further, the minutes shall disclose the particulars of the directors who attended the meeting through video conferencing or other audio-visual means.

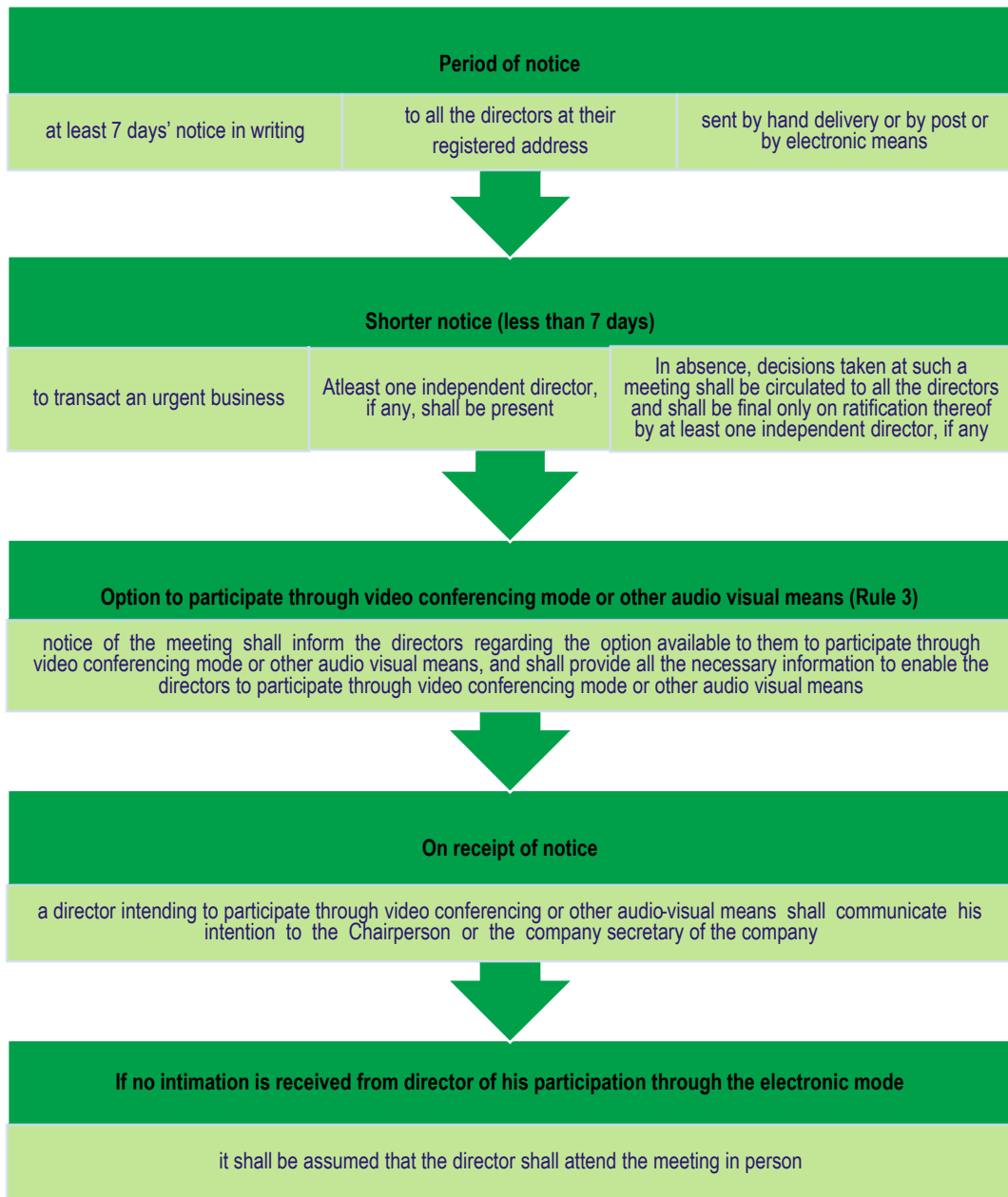
15.	Circulation of draft minutes of the meeting	The draft minutes of the meeting shall be circulated among all the directors within 15 days of the meeting either in writing or in electronic mode as may be decided by the Board.
16.	Confirmation or written comments about the accuracy of recording of the proceedings	Every director who attended the meeting, whether personally or through video conferencing or other audio-visual means, shall confirm or give his comments in writing, about the accuracy of recording of the proceedings of that particular meeting in the draft minutes, within seven days or some reasonable time as decided by the Board, after receipt of the draft minutes failing which his approval shall be presumed.
17.	After completion of meeting	Minutes shall be entered in the minute book signed by the Chairperson

Explanation-For the purposes of this rule, "video conferencing or other audio visual means" means audio- visual electronic communication facility employed which enables all the persons participating in a meeting to communicate concurrently with each other without an intermediary and to participate effectively in the meeting.

Requirement of attending all the Board Meetings:

Is it necessary for all the directors to attend all the Board meetings of the company held during a year? Apparently, the answer is no because it shall be illogical to expect from every director to attend each and every meeting but as they are the guardians of the company they must try their best to attend as many Board meetings as possible. However, a continuous absence is also detrimental if we look at Section 167 (1) (b) which states that a director shall be required to vacate his office if he absents himself from all the meetings of the Board of Directors held during a period of 12 months with or without seeking leave of absence of the Board.

(iv) Notice of the Board meeting [Section 173 (3)]:



- (v) **Penalty for failure to give notice:** Section 173(4) prescribes a penalty of ₹ 25,000 in respect of every officer⁴ of the Company whose duty is to give notice under Section 173 and who has failed to do so.

⁴According to Secretarial Standard 1 (SS-1), any Director of a company may, at any time, summon a Meeting of the Board, and the Company Secretary or where there is no Company Secretary, any person authorised

Example 2: The Board of Directors of Infotech Consultants Limited, registered in Kolkata, proposes to hold the next board meeting in the month of May, 2019. It was decided to hold board meeting in Chennai through video conferencing, though all the directors of the company reside at Kolkata. As provision in the Companies Act, 2013 does not require that the board meetings must be held at a particular place. Accordingly, there is no difficulty in holding the current board meeting at Chennai through video conferencing even if all the directors of the company reside at Kolkata and the registered office is also situated at Kolkata. However, it is to be seen that the legal requirements as prescribed by Section 173 (2) and Rule 3 of the Companies (Meetings of Board and its Powers) Rules, 2014 are meticulously followed.

Example 3: XYZ Ltd. is a foreign collaborator in ABC Ltd. incorporated in India under the Companies Act, 2013. The foreign collaborator holds 49% of the shareholding. The Board meetings of ABC Ltd are usually held in India and sometimes meetings of the Board are called at a very short notice for which there is a provision in the Articles of Association that during such situations, notices of the meetings of the Board can be sent by e-mail. Here in the given instance, such a provision in the Articles of Association of ABC Ltd. is valid.

In terms of the proviso to section 173(3) of the Companies Act, 2013 a meeting of the Board may be called at shorter notice to transact urgent business subject to the condition that at least one independent director, if any, shall be present at the meeting. No exception is made for any class or classes of companies.

Further, under section 173(3) a meeting of the Board shall be called by giving not less than seven days' notice in writing to every director at his address registered with the company and such notice shall be sent by hand delivery or by post or by electronic means.

If we examine the above provision, it is amply clear that the notice is allowed to be sent, *inter-alia*, by electronic means also. Hence, the sending of notice by e-mail is a permissible mode of delivery and can be resorted to without any hindrance. In case Articles contain such a provision, there is no illegality involved even if there is a foreign collaborator in the company.

Therefore, in the given case the shorter notice by e-mail is legally permitted. It is to be noted that there should be the presence of quorum and at least one independent director at the meeting. The provision of the Articles in this regard is not so relevant since the position is quite clear in the Act itself.

In an order given by NCLAT, New Delhi in *Achintya Kumar Barua alias Manju Baruah v. Ranjit Barthkur*, was held that section 173(2) gives right to a director of company to participate in board meeting through video-conferencing or other audio-visual means. Tribunal allowed application of respondent director seeking facility of attending board meeting through video-conferencing.

by the Board in this behalf, on the requisition of a Director, shall convene a Meeting of the Board, in consultation with the Chairman or in his absence, the Managing Director or in his absence, the Whole-time Director, where there is any, unless otherwise provided in the Articles.

Appellant director raised a apprehension that it would not be possible to ensure that no person other than concerned director was attending said meeting. According to appellant, Secretarial Standards on Meetings of Board of Directors have prescribed that such option under provisions of 2013 Act and Rules should be resorted to only when facilities were provided by Company to its Directors. In instant case company had all necessary infrastructure available for conducting meeting through video-conferencing, it was held to follow provisions of section 173 as it would be in interest of Companies as well as directors and it would not be appropriate to shut-out these provisions on mere apprehensions.



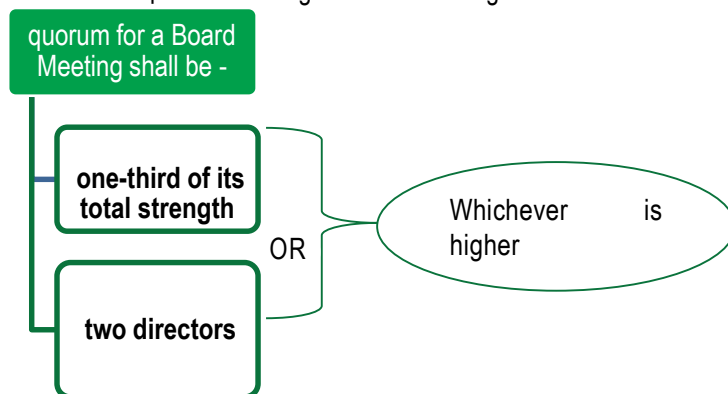
3. QUORUM FOR MEETINGS OF BOARD [SECTION 174]

A quorum is the minimum number of directors who must attend the proceedings in order to transact business validly at a duly convened Board meeting. The directors must not be disqualified to participate in the meeting. Unless the quorum is present at the meeting, it shall not be deemed to have been properly held.

Section 174 of the Companies Act, 2013 contains provisions in respect of quorum required for the meetings of the Board of Directors. These provisions are discussed as under:

(i) **Quorum for a Board Meeting [Section 174 (1)]:** In respect of quorum for Board meeting following points are noteworthy:

- The quorum for a Board Meeting shall be **one-third of its total strength or two directors**, whichever is **higher**.
- While calculating the quorum, any fraction of a number shall be rounded off as one.
- The total strength shall not include those directors whose places are vacant.
- The quorum needs to be present throughout the meeting.



It may be noted that the articles of a company cannot specify a quorum which is less than that prescribed by Section 174 (1). However, there is no bar in fixing a higher quorum than required statutorily.

Modification

*In case of a **Section 8 Company**, Section 174 (1) stands modified to state that quorum shall be either **eight members or 25% of its total strength whichever is less**, provided that the quorum shall not be less than two members.*

The above modification is applicable subject to the condition that the Section 8 company has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar. [Notification No. G.S.R.466(E), dated 5th June, 2015 as amended by the Notification No. G.S.R.584 (E), dated 13th June, 2017.]

- (ii) **Participation through electronic means to be counted for Quorum:** The directors who participate by video conferencing or other audio-visual means shall also be counted for the purpose of determining the quorum at the meeting **unless** they are to be excluded for any items of business under any provisions of the Act or the rules⁵.

- (iii) **In case when there is vacancy in the Board [Section 174 (2)]:** In case there is any vacancy in the Board (*i.e.* strength is less than that mentioned in the Articles), the continuing directors may act irrespective of such vacancy.

However, the problem will arise when due to such vacancy/ies the number of directors is reduced below the quorum fixed by the Companies Act, 2013.

If this is the situation, the continuing directors or director may act for the following purposes only and nothing else:

- (a) to increase the number of directors to that fixed for the quorum *i.e.* appoint additional director; or
 - (b) to summon a general meeting of the company.
- (iv) **Quorum in case of interested directors [Section 174 (3)]:** Where at any time the number of interested directors exceeds or is equal to two-thirds of the total strength of the Board of Directors, the quorum shall be the number of non-interested directors who are present at the meeting; but their number must not be less than two. While calculating the quorum, any fraction of a number shall be rounded off as one.

Meaning of Interested Director: The term “Interested director” for the purposes of Section 174 (3) means a director within the meaning of Section 184 (2).

According to Section 184(2) “**interested director**” means every director of a company who is in any way, whether directly or indirectly, concerned or interested in a contract or arrangement or proposed contract or arrangement entered into or to be entered into—

- (a) with a body corporate in which such director or such director in association with any other director, holds **more than two per cent** shareholding of that body corporate, or is a promoter, manager, Chief Executive Officer of that body corporate; or

⁵ As per Explanation to Rule 3 (5) (a) of the Companies (Meetings of Board and its Powers) Rules, 2014.

- (b) with a firm or other entity in which, such director is a partner, owner or member, as the case may be.

Exception

*In case of a **private company** which has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar, the provisions of Section 174(3) shall apply with the exception that the interested director may participate in such meeting after disclosure of his interest pursuant to Section 184. [Notification No. G.S.R. 464(E) dated 5th June 2015 as amended by Notification No. G.S.R. 583 (E) dated 13th June, 2017]*

- (v) **Adjournment of meeting which could not be held for want of quorum:** As we have noticed that a Board meeting cannot be validly held if there is no quorum present. Thus, where a meeting of the Board could not be held for want of quorum, then, unless the articles of the company otherwise provide, the meeting shall automatically stand adjourned to the same day at the same time and place in the next week or if that day is a national holiday, till the next succeeding day, which is not a national holiday, at the same time and place.
- (vi) **Exemption to OPC:** According to Proviso to Section 173 (5), the provisions of Section 174 relating to quorum are not applicable to such One Person Company (OPC) which has only one director on its Board.

Example 4: There are 9 directors in a company and out of which 2 offices of the directors have fallen vacant. According to section 174(1) of the Companies Act, 2013, quorum is one third of the total strength of Board (any fraction contained in the said one third being rounded off as one) or two directors whichever is higher. The total strength is to be derived after deducting the number of directors whose offices are vacant. Therefore, where total number of directors is 9 and 2 offices of the directors have fallen vacant; the total strength comes to seven. In this case $1/3$ of $7 = 2\frac{1}{3}$ directors which will be rounded off as 3 which is higher than 2. Therefore, 3 directors would constitute the quorum for the Board meetings here.

Now, if suppose, there are total 15 directors in a company and during discussion on a particular item, 13 of the directors happen to be 'interested' within the meaning of section 184(2) of the Companies Act, 2013. Under section 174(3) of the Companies Act, 2013, if at any time the number of the interested directors exceeds or is equal to two thirds of the total strength of the Board of Directors, the number of the directors who are non-interested but present at the meeting, not being less than two shall constitute the quorum.

In the given situation, there are total 15 directors and the Board meeting commences with all of them. During the meeting, an item comes up for discussion in respect of which 13 directors happen to be 'interested directors'. In spite of the fact that the interested directors are more than two-thirds, minimum two non-interested directors who are present at the meeting shall constitute the quorum and they can validly transact that particular item of business in view of Section 174 (3).

Example 5: A meeting of the Board of 'No Holiday Ltd' was held on a holiday on account of Ganesh Chaturthi. However due to lack of quorum, the proceedings of the meeting could not be held and therefore the Chairman of the meeting with the consent of the majority decided that the Board meeting be adjourned to next week on the same day. However, the date fixed for the adjourned meeting happened to be a Sunday. In such case, where a board meeting is adjourned due to lack of quorum, then under section 174(4) the adjourned meeting can be held on the same day at the same time and place in the next week or if that day is a national holiday, till the next succeeding day, which is not a national holiday, at the same time and place, unless the Articles provide otherwise.

Since Section 174(4) specifies exclusion of only a national holiday, any original/adjourned/committee meetings can be held on Sundays and other holidays. In view of this provision, the adjourned meeting of the Board of 'No Holiday Ltd' can be held on Sunday without involvement of any illegality.

High Court of Andhra Pradesh, in *Smt. Dr. Renuka Datla v. Biological E Ltd.* in an appeal held that where with resignation of one director, number of Directors fell below minimum number of two as prescribed under section 174, subsequent Board meeting convened and conducted by said director by his withdrawal of resignation was patently illegal and consequently, further appointments of directors in such meetings were also illegal and non-est.

In the said case, three persons, constituted Board of Directors of company. One of directors died. Another director R5 submitted resignation from directorship and, thus, only one director was left on Board. However, R5 withdrew his resignation and on same date called upon a Board meeting. Whether with resignation of R5 as a Director, company failed to satisfy mandatory provisions of section 174 of having atleast two directors and with resignation of R5 coming into force with immediate effect as desired by him, he had no authority to convene any board meetings. It was held, that meetings of Board of Directors could not be said to be validly held and, thus, appointment of new directors in said meeting was also invalid.



4. PASSING OF RESOLUTION BY CIRCULATION [SECTION 175]

Section 175 of the Act and Rule 5 of the Companies (Meetings of Board and its Powers) Rules, 2014, contain provisions for passing of resolutions by circulation. Normally, a board meeting is conducted to pass resolutions. There are certain matters, which according to the provisions of the Companies Act, 2013, can only be considered and decided at the duly convened board meetings and therefore, they cannot be implemented through passing resolutions by circulation. However, in cases where the matter is not that much important and therefore, does not require its consideration at a board meeting though consent of directors is required to implement that matter or the calling of board meeting is a lengthy and costly affair keeping in view the urgent implementation of certain decisions, the company may, in respect of such matters, resort to passing of resolutions by

circulation. As a matter of fact, all such matters which do not require consideration at a board meeting can be decided through resolutions which are passed by circulation.

The provisions of Section 175 and Rule 5 are discussed as under:

- (i) **Requirements to pass resolution by circulation [Section 175 (1)]:** A resolution shall be deemed to have been duly passed by the Board or by a committee thereof by circulation in case:

the resolution has been circulated in draft, together with the necessary papers, if any, to all the directors, or members of the committee, as the case may be,

at their addresses registered with the company in India,

by hand delivery or by post or by courier, or through such electronic means as may be prescribed, and

and has been approved by a majority of the directors or members, who are entitled to vote on the resolution.

Rule 5 provides that a resolution in draft form may be circulated to the directors together with the necessary papers for seeking their approval, by electronic means which may include e-mail or fax.

- (ii) **When a resolution cannot be passed by circulation [Proviso to Section 175 (1)]:** If at least 1/3rd of the total number of directors of the company for the time being require that any resolution under circulation must be decided at a meeting, the chairperson shall put the resolution to be decided at a meeting of the Board (instead of being decided by circulation).
- (iii) **Noting of passed resolution in next meeting [Section 175 (2)]:** A resolution that has been passed by circulation shall have to be necessarily noted in the next meeting of board or the committee thereof, as the case may be, and made part of the minutes of such meeting.

Example 6: In respect of certain matter which did not require to be decided at a board meeting, PQR Ltd. thought it prudent to pass resolution thereof by circulation. Accordingly, a draft resolution was circulated among all the six directors by e-mail. Three directors did not give their consent and desired that the resolution was required to be decided at a meeting.

In the light of the Proviso to Section 175 (1) where minimum 1/3rd of the total number of directors require that any resolution under circulation must be decided at a meeting, the Chairperson shall put the resolution to be decided at a meeting of the Board. In the given case, one-half of the total number of directors (*i.e.* three out of six) requires that the resolution must be decided at a Board meeting. Since their counting is more than one-third of total strength, the Chairperson needs to take the call and put the resolution to be decided at a duly convened meeting of the Board.



5. AUDIT COMMITTEE, VIGIL MECHANISM AND PUNISHMENT [SECTION 177 AND SECTION 178 (8)]

A. AUDIT COMMITTEE

Section 177 of the Act and Rules 6 and 6A of the Companies (Meetings of Board and its Powers) Rules, 2014, contain provisions in respect of Audit Committee. These provisions are described as under:

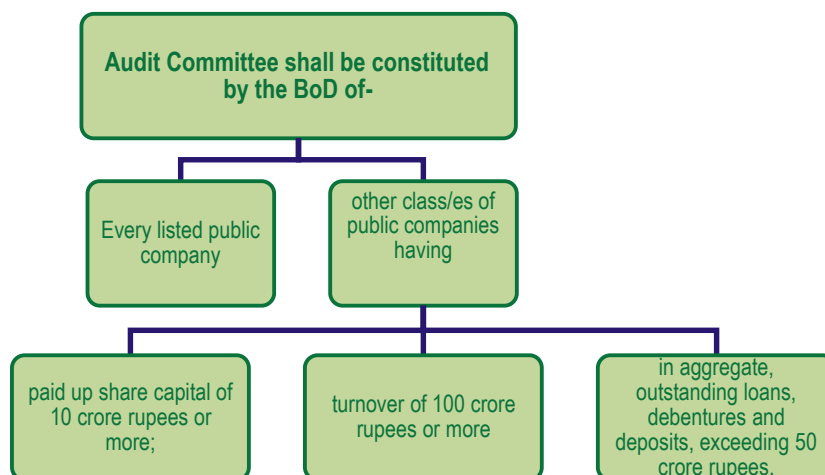
(i) Companies required to constitute an Audit Committee [Section 177 (1) and Rule 6]:

Following companies are required to constitute an Audit Committee:

- (a) every listed public company;
- (b) public companies having paid up share capital of 10 crore rupees or more;
- (c) public companies having turnover of 100 crore rupees or more;
- (d) public companies which have, in aggregate, outstanding loans, debentures and deposits, exceeding 50 crore rupees.

Note: The public companies stated at points (b),(c) and (d) are the classes of companies which are prescribed by Rule 6 of the Companies (Meetings of Board and its Powers) Rules, 2014 and are required to constitute an Audit Committee.

In fact, Rule 6 requires that the companies prescribed in Rule 4 of the Companies (Appointment and Qualifications of Directors) Rules, 2014 are the companies which shall constitute an Audit Committee.



Companies not required constituting an Audit Committee: Following unlisted companies are not covered by Rule 4 (1) of the Companies (Appointment and Qualifications of Directors) Rules, 2014; and therefore, are not required to constitute an Audit Committee:

- (a) a joint venture;
- (b) a wholly owned subsidiary; and
- (c) a dormant company as defined under Section 455 of the Act.

When a company ceases to constitute an Audit Committee: A company which was obligated to constitute an Audit Committee, shall not be required to constitute such Audit Committee if it ceases to fulfill any of the three conditions relating to paid-up share capital or turnover or outstanding loans, etc. [as laid down in Third Proviso to Rule 4 (1)⁶] for **three consecutive years**. It shall again be required to constitute an Audit Committee if it starts meeting any of such conditions.

Clarification: *Explanation* to Rule 4 (1)⁷ clarifies that the paid-up share capital or turnover or outstanding loans, debentures and deposits, as the case may be, as existing on the last date of latest audited financial statements shall be taken into account.

- (ii) **Composition of an Audit committee:** According to Section 177 (2), the Audit Committee shall consist of a minimum of 3 directors with independent directors forming a majority.

Further, it is required that the majority of members of the Audit Committee including its Chairperson shall be persons with ability to read and understand the financial statement.

*Vide Notification No. G.S.R. 466(E), dated 05-06-2015 as amended by Notification No. G.S.R. 584 (E), dated 13-06-2017, in case of **Section 8 Companies**, the requirement of Section 177 (2) i.e. while constituting an Audit Committee, the 'Independent Directors' shall form a majority, shall not apply provided such a company has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar.*

- (iii) **Disclosure of composition of Audit Committee [Section 177(8)]:** The Board's report under Section 134 (3) shall disclose the composition of an Audit Committee.

In case, where the Board had not accepted any recommendation of the Audit Committee, the same shall also be disclosed in the Board's report along with the reasons therefor.

- (iv) **Responsibilities of the Audit Committee:** According to Section 177 (4), every Audit Committee shall act in accordance with the terms of reference specified in writing by the Board which shall, *inter alia*, include,-

- (a) recommendation for appointment, remuneration and terms of appointment of auditors of the company;

⁶Rule 4 (1) of the Companies (Appointment and Qualifications of Directors) Rules, 2014

⁷Rule 4 (1) of the Companies (Appointment and Qualifications of Directors) Rules, 2014

*In case of a **Government company** which has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar, for the words “recommendation for appointment, remuneration and terms of appointment” used in Section 177 (4) (i), the words “**recommendation for remuneration**” shall be substituted- Notification No. G.S.R. 463(E), dated 05.06.2015 as amended by Notification No. G.S.R. 582 (E), dated 13.06.2017.*

- (b) review and monitor the auditor’s independence and performance, and effectiveness of audit process;
- (c) examination of the financial statement and the auditors’ report thereon;
- (d) approval or any subsequent modification of transactions of the company with related parties. The provisos to this clause are stated below:

Omnibus approval: It is provided that the Audit Committee may make omnibus approval for related party transactions proposed to be entered into by the company subject to such conditions as prescribed under Rule 6A (refer the Box below);

Conditions prescribed under Rule 6A of the Companies (Meetings of Board and its Powers) Rules, 2014 for Omnibus Approval for Related Party Transactions on Annual Basis

According to Rule 6A, all related party transactions shall require approval of the Audit Committee. The Audit Committee may make omnibus approval for related party transactions proposed to be entered into by the company subject to the following conditions:

- (1) The Audit Committee shall, after obtaining approval of the Board of Directors, specify the **criteria for making the omnibus approval** which shall include the following:
 - (a) **maximum value of the transactions**, in aggregate, which can be allowed under the omnibus route in a year;
 - (b) **the maximum value per transaction** which can be allowed;
 - (c) extent and manner of **disclosures** to be made to the Audit Committee at the time of seeking omnibus approval;
 - (d) **review**, at such intervals as the Audit Committee may deem fit, related party transaction entered into by the company pursuant to each of the omnibus approval made;
 - (e) **transactions which cannot** be subject to the omnibus approval by the Audit Committee.
- (2) The Audit Committee shall **consider the following factors** while specifying the criteria for making omnibus approval: -

- (a) repetitiveness of the transactions (in past or in future);
- (b) justification for the need of omnibus approval.
- (3) The Audit Committee shall satisfy itself on the need for omnibus approval for transactions of repetitive nature and that such approval is in the interest of the company.
- (4) The omnibus approval shall contain or indicate the following: -
 - (a) name of the related parties;
 - (b) nature and duration of the transaction;
 - (c) maximum amount of transaction that can be entered into;
 - (d) the indicative base price or current contracted price and the formula for variation in the price, if any; and
 - (e) any other information relevant or important for the Audit Committee to take a decision on the proposed transaction:

However, where the need for related party transaction cannot be foreseen and aforesaid details are not available, audit committee may make omnibus approval **for such** transactions subject to their value not exceeding rupees one crore per transaction.
- (5) Omnibus approval shall be valid for a period not exceeding **one financial year** and shall require fresh approval after the expiry of such financial year.
- (6) Omnibus approval shall not be made for transactions in respect of selling or disposing of the undertaking of the company.
- (7) Any other conditions as the Audit Committee may deem fit.

If no approval accorded: It is further provided that in case of a transaction (which is not a transactions referred to in section 188), where Audit Committee does not approve such transaction, it shall make its recommendations to the Board.

Voidable transaction: In case of a transaction which does not involve an amount exceeding one crore rupees and which is entered into by a director or officer of the company without obtaining the approval of the Audit Committee and if it is not ratified by the Audit Committee **within three months** from the date of the transaction, such transaction shall be voidable at the option of the Audit Committee. In case such transaction is with the related party to any director or is authorised by any other director, the director concerned shall indemnify the company against any loss incurred by it.

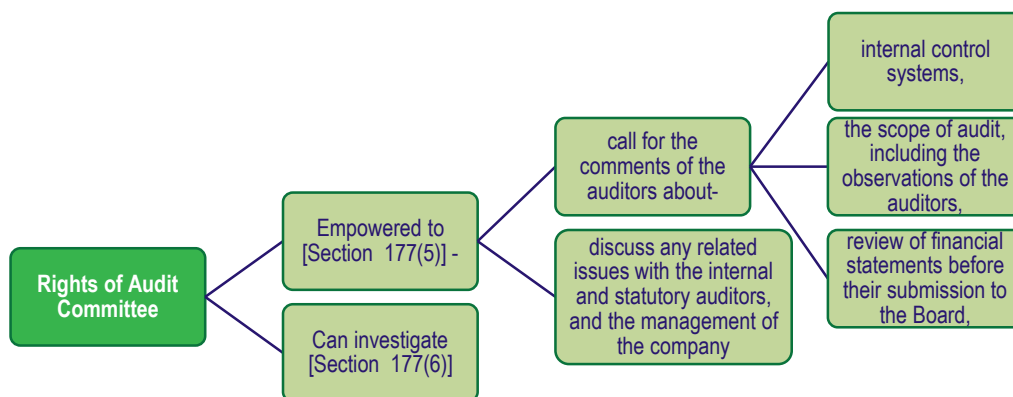
Non-applicability to a transaction between a holding and its wholly owned subsidiary company: It is also provided that the provisions of this clause shall not

apply to a transaction, other than a transaction referred to in Section 188, between a holding company and its wholly owned subsidiary company.

- (e) scrutiny of inter-corporate loans and investments;
- (f) valuation of undertakings or assets of the company, wherever it is necessary;
- (g) evaluation of internal financial controls and risk management systems;
- (h) monitoring the end use of funds raised through public offers and related matters.

(v) Rights of the Audit Committee:

- (a) The Audit Committee may **call for the comments of the auditors** about internal control systems, the scope of audit, including the observations of the auditors. It shall have right to review the financial statements before their submission to the Board. It may also discuss any related issues with the internal and statutory auditors and the management of the company. [Section 177(5)]
- (b) The Audit Committee shall have **authority to investigate** into any matter in relation to the items specified in sub-section (4) or referred to it by the Board and for this purpose shall have power to obtain professional advice from external sources and have full access to information contained in the records of the company. [Section 177(6)]



- (vi) Right to be heard before the Audit Committee:** The **auditors** of a company and the **key managerial personnel** shall have a right to be heard in the meetings of the Audit Committee when it considers the **auditor's report** but shall not have the right to vote. [Section 177(7)]

B. VIGIL MECHANISM

A 'vigil mechanism' is formed for the directors and employees who may report genuine concerns. Not all the companies but only the prescribes ones are required to establish 'vigil mechanism'. The

provisions contained in Section 177 (9) and (10) and Rule 7 of the Companies (Meetings of Board and its Powers) Rules, 2014 govern the concept of 'vigil mechanism'. These are stated below:

(i) **Formation of Vigil Mechanism (VM):**

According to Section 177(9),
VM shall be formed by -

- every listed company
- prescribed class of companies as per Rule 7
- the Companies which accept deposits from the public;
- the Companies which have borrowed money from banks and public financial institutions in excess of 50 crore rupees.

(ii) **Purpose of Vigil Mechanism [Section 177 (9)]:** A vigil mechanism is formed for the directors and employees who may report genuine concerns in the manner prescribed in Rule 7.

(iii) **Vigil Mechanism to ensure adequate safeguards:** According to Section 177 (10), the vigil mechanism shall provide for adequate safeguards against victimisation of persons who use such mechanism and make provision for direct access to the Chairperson of the Audit Committee in appropriate or exceptional cases.

(iv) **Establishment of Vigil Mechanism and Manner of Reporting:** The provisions of Rule 7 in this respect are stated as under:

- (1) **Users of Vigil Mechanism:** The directors and employees of the company can use the system of vigil mechanism for reporting their genuine concerns.
- (2) **Companies having Audit Committee:** The companies which are required to constitute an audit committee shall oversee the vigil mechanism through the audit committee and if any of the members of the committee have a conflict of interest in a given case, they should recuse themselves and the others on the committee would deal with the matter on hand.
- (3) **Companies having no Audit Committee:** In case of other companies, the Board of Directors shall nominate a director to play the role of audit committee for the purpose of vigil mechanism. Other directors and employees may report their concerns to such nominated director.
- (4) **Adequate safeguards against victimisation:** As stated in Section 177 (10), the vigil mechanism shall provide for adequate safeguards against victimisation of employees and directors who avail of it.
- (5) **Direct access in exceptional cases:** As stated in Section 177 (10), the employees and directors who avail of vigil mechanism may have direct access to the Chairperson of the Audit Committee or the director nominated to play the role of Audit Committee, as the case may be, in exceptional cases.

- (6) **Action against repeated frivolous complaints:** In case of repeated frivolous complaints being filed by a director or an employee, the audit committee or the director nominated to play the role of audit committee may take suitable action against the concerned director or employee including reprimand.
- (v) **Disclosure of details of vigil mechanism [Section 177 (10)]:** It is imperative for the company to disclose the details of the establishment of vigil mechanism on the website of the company and in Board's report.

C. PUNISHMENT FOR CONTRAVENTION OF SECTION 177 [Section 178(8)]: In case of contravention of Section 177, the company shall be liable to a penalty of five lakh rupees and every officer of the company who is in default shall be liable to a penalty of one lakh rupees.

Note: In the case of a listed company, the formation, composition, responsibilities and rights of Audit Committee shall be governed by SEBI (LODR) Regulations issued under the SEBI Act, 1992.



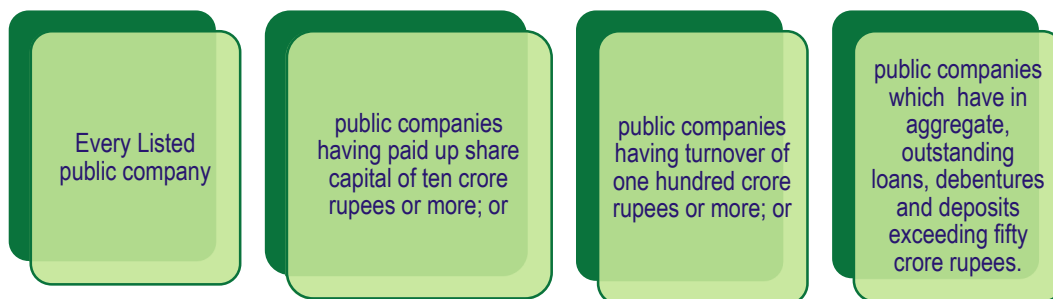
6. NOMINATION AND REMUNERATION COMMITTEE AND STAKEHOLDERS RELATIONSHIP COMMITTEE AND PUNISHMENT [SECTION 178]

Section 178 of the Act, contains provisions in respect of Nomination and Remuneration Committee as well as Stakeholders Relationship Committee.

A. NOMINATION AND REMUNERATION COMMITTEE (NRC)

Sub-sections (1) to (4) of Section 178 and Rule 6 of the Companies (Meetings of Board and its Powers) Rules, 2014 lay down the provisions in respect of the Nomination and Remuneration Committee as under:

- (i) **Formation of Nomination and Remuneration Committee :** Section 178 (1) read with Rule 6 state that the Board of directors of every listed public company and a company covered under Rule 4 of the Companies (Appointment and Qualification of Directors) Rules, 2014, shall constitute a Nomination and Remuneration Committee. Following diagram depicts the prescribed companies which are required to constitute the Nomination and Remuneration Committee:



Companies not required to constitute a Nomination and Remuneration Committee:

Following unlisted companies are not covered by Rule 4 (1) of the Companies (Appointment and Qualification of Directors) Rules, 2014; and therefore, are not required to constitute a Nomination and Remuneration Committee:

- (a) a joint venture;
- (b) a wholly owned subsidiary; and
- (c) a dormant company as defined under Section 455 of the Act.

When a company ceases to constitute a Nomination and Remuneration Committee: A company which was obligated to constitute a Nomination and Remuneration Committee, shall not be required to constitute such Committee if it ceases to fulfill any of the three conditions relating to paid-up share capital or turnover or outstanding loans, etc. [as laid down in Third Proviso to Rule 4 (1)⁸] for **three consecutive years**. It shall again be required to constitute a Nomination and Remuneration Committee if it starts meeting any of such conditions.

Clarification: Explanation to Rule 4 (1)⁹ clarifies that the paid-up share capital or turnover or outstanding loans, debentures and deposits, as the case may be, as existing on the last date of latest audited financial statements shall be taken into account.

(ii) Composition of Nomination and Remuneration Committee:

- (a) The NRC shall consist of **3 or more non-executive directors** out of which not less than one-half shall be independent directors.
- (b) The Chairperson (whether executive or non-executive) of the company shall not chair such a committee. However, he may be appointed as a member of the committee.

(iii) Functions of the Nomination and Remuneration Committee: The various functions of NRC shall be as under:

- (a) **Formulation of criteria for qualifications, etc.:** The NRC shall formulate the criteria for determining qualifications, positive attributes and independence of a director [Sub section (3)].
- (b) **Recommendation of Policy regarding remuneration:** The NRC shall recommend to the Board a policy, relating to the remuneration for the directors, key managerial personnel and other employees [Sub section (3)].
- (c) **Recommendation for appointment and removal:** The NRC shall identify persons who are qualified to become directors and who may be appointed in senior management in accordance with the criteria laid down, recommend to the Board their appointment and removal. [Sub-section (2)]

⁸Rule 4 (1) of the Companies (Appointment and Qualification of Directors) Rules, 2014

⁹Rule 4 (1) of the Companies (Appointment and Qualification of Directors) Rules, 2014

Note: The expression “**senior management**” means personnel of the company who are members of its core management team excluding Board of Directors comprising all members of management one level below the executive directors, including the functional heads.

- (d) **Manner for effective evaluation of performance:** The NRC shall specify the manner for effective evaluation of performance of Board, its committees and individual directors to be carried out either by the Board, by the Nomination and Remuneration Committee or by an independent external agency and review its implementation and compliance.
- (e) **Parameters for formulation of Policy:** According to Section 178(4), the Nomination and Remuneration Committee shall, while formulating the policy under Section 178 (3) ensure that—
- the level and composition of remuneration is reasonable and sufficient to attract, retain and motivate directors of the quality required to run the company successfully;
 - relationship of remuneration to performance is clear and meets appropriate performance benchmarks; and
 - remuneration to directors, key managerial personnel and senior management involves a balance between fixed and incentive pay reflecting short and long-term performance objectives appropriate to the working of the company and its goals.
- (f) **Disclosure regarding policy:** It is imperative that such policy [i.e. policy formulated under Section 178 (3)] shall be placed on the **website** of the company, if any, and the salient features of the policy and changes therein, if any, along with the web address of the policy, if any, shall be disclosed in the **Board's report**.
- (iv) **Attending of general meetings [Section 178 (7)]:** The Chairperson or in his absence, any other member of the committee authorised by him in this behalf shall attend the general meetings of the company.

Note: In the case of a listed company, formation, composition, responsibilities and rights of Nomination and Remuneration Committee shall be governed by SEBI (LODR) Regulations issued under SEBI Act, 1992. According to the listing agreement, the members of the NRC shall be non-executive directors and the Chairperson needs to be an independent director.

Modification

*In case of a **Government company** which has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar, Sub-sections (2), (3) and (4) of Section 178, shall not apply except with regard to appointment of 'senior*

management' and other employees. - Notification No. G.S.R. 463 (E), dated 05-06-2015 as amended by Notification No. G.S.R. 582 (E), dated 13-06-2017.

B. STAKEHOLDERS RELATIONSHIP COMMITTEE (SRC)

Formation and functioning of SRC: Section 178 (5) and (6) lay down the provisions relating to the formation, constitution and functioning of the Stakeholders Relationship Committee as under:

Sl. No.	Section	With respect to	Provisions says
(i)	178 (5)	Formation and constitution of Stakeholders Relationship Committee (SRC)	The Board of Directors of a company which consists of more than 1000 shareholders, debenture-holders, deposit-holders and any other security holders at any time during a financial year shall constitute a Stakeholders Relationship Committee.
(ii)	178 (5)	Chairperson of Stakeholders Relationship Committee (SRC)	SRC shall be headed by a Chairperson who shall be a non-executive director. Further, SRC shall consist of such other members as may be decided by the Board.
(iii)	178 (6)	Objective of the Stakeholders Relationship Committee (SRC)	SRC shall consider and resolve the grievances of security holders of the company. It shall protect the interests of all security holders and not merely of the equity investors.

Chairperson of committees to attend the general meetings : As per section 178(7), the **chairperson** of each of the committees constituted under this section or, in his absence, **any other member** of the committee authorised by him in this behalf shall attend the general meetings of the company.

C. PENALTY FOR CONTRAVENTION [Section 178(8)]: In case of contravention of provisions of Section 178, the company shall be liable to a penalty of five lakh rupees and every officer of the company who is in default shall be liable to a penalty of one lakh rupees.

No contravention if SRC is unable to resolve in good faith: It is to be noted that inability to resolve or consider any grievance by the Stakeholders Relationship Committee **in good faith** shall not constitute a contravention of Section 178; and therefore, **no penalty** shall be attracted. [refer Proviso to Section 178 (8)].

Note: In the case of a listed company, formation, composition, responsibilities and rights of Stakeholder Relationship Committee shall be governed by SEBI (LODR) Regulations, 2015 issued under SEBI Act, 1992.

Exemption

*Section 178 of the Act shall not apply to a **Section 8 company** provided it has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar - Notification No. G.S.R. 466 (E), dated 05-06-2015 as amended by Notification No. G.S.R. 584 (E), dated 13-06-2017.*

**7. POWERS OF THE BOARD [SECTION 179]**

Section 179 of the Act and Rule 8 of the Companies (Meetings of Board and its Powers) Rules, 2014 lay down the provisions in respect of powers of the Board. They are described as under:

- (i) **BoD is entitled to exercise the same powers as the company is authorised:** According to Section 179 (1), the Board shall be entitled to exercise all such powers as the company is authorised to exercise; and to do all such acts and things which the company is authorised to do.

In fact, the Board of Directors of a company enjoy wide-ranging powers; virtually all the powers for managing the affairs of the company except where the given matters require approval of shareholders in general meetings. In other words, the Board is empowered to exercise all such powers which shall secure the interests of the company and the shareholders.

- (ii) **Placing of restrictions on exercising of powers by the Board [Provisos to Section 179 (1)]:**
- (a) The exercise of powers by the Board of Directors is not unbridled or unrestricted. It is provided that while exercising such power or doing such act or thing, the Board shall be subject to the provisions contained in that behalf in the Companies Act, 2013, or in the memorandum or articles, or in any regulations which are not inconsistent with the Act or memorandum or articles and are duly made thereunder. This will include regulations made by the company in general meeting.
 - (b) Further, the Board shall not exercise any power or do any act or thing which is directed or required, whether under the Companies Act, 2013 or by the memorandum or articles of the company or otherwise, to be exercised or done by the company in general meeting.
- (iii) **Prospective effect of regulation made in general meeting [Section 179 (2)]:** Any regulation made by the company in general meeting shall not invalidate any prior act of the Board which would have been valid if that regulation had not been made.

Thus, a regulation made by a company in general meeting cannot have retrospective effect and therefore, cannot invalidate prior acts of the Board if they were otherwise validly executed earlier.

(iv) **Powers of Board to be exercised by means of resolutions [Section 179 (3)]**: Following powers are required to be exercised by the Board of Directors by means of the resolutions passed at a duly convened Board meeting:

- (a) to **make calls on shareholders** in respect of money unpaid on their shares;
- (b) to **authorise buy-back of securities** under Section 68;
- (c) to **issue securities**, including debentures, whether in India or outside India;
- (d) to **borrow monies**;

Note: By way of Explanation II, it is clarified that in respect of dealings between a company and its bankers, the exercise of the power by the company specified in clause (d) above shall mean the arrangement made by the company with its bankers for the **borrowing of money** by way of overdraft or cash credit or otherwise. This does not refer to the actual day-to-day operation on overdraft, cash credit or other accounts by means of which the arrangement so made is actually availed of.

- (e) to **invest the funds** of the company. *[Section 186 (5) requires this power to be exercised by a Board resolution which is passed with the consent of all the directors present at the Board meeting];*
- (f) to **grant loans or give guarantee or provide security** in respect of loans. *[Section 186 (5) requires this power to be exercised by a Board resolution which is passed with the consent of all the directors present at the Board meeting];*

Exemption

*In respect of a **Section 8 Company** which has not committed a default in filing its financial statements under Section 137 or Annual Return under section 92 with the Registrar, the matters referred to in clauses (d), (e), and (f) of Sub-section (3) of Section 179 may be decided by the Board by **circulation** instead of at a meeting.*

[Notification No. GSR 466 (E), dated 05-06-2015 as amended by Notification No. GSR 584 (E), dated 13-06-2017]

- (g) to **approve financial statement and the Board's report**;
- (h) to **diversify the business** of the company;
- (i) to **approve amalgamation, merger or reconstruction**;
- (j) to **take over** a company or **acquire a controlling or substantial stake** in another company;

(k) **other matters** as prescribed in Rule 8 of the Companies (Meetings of Board and its Powers) Rules, 2014. These matters, also to be exercised only by means of resolutions passed at the meetings of the Board, are:

- (1) to make **political contributions**;
- (2) to **appoint or remove key managerial personnel (KMP)**;
- (3) to **appoint internal auditors and secretarial auditor**.

Note: It is to be noted that the above list is not exhaustive. There are certain other powers which are also to be exercised by the Board of Directors at a duly convened board meeting. Some of them are as under:

- Making of **contributions to political parties** under Section 182
- **Filling of casual vacancy** under Section 161 (4) when the office of a director appointed in the general meeting falls vacant before the expiry of his term in the normal course.
- **Approving of transactions with related parties** as provided under Section 188.
- **Giving of loans or making of investment** in the shares of other body corporates as provided under Section 186. In this case, besides passing the resolution at a board meeting, consent of all the directors present at the meeting is also required.
- **Appointing a person as a managing director** who is also holding office of managing director or manager in another company as provided under Section 203. This power is to be exercised with the consent of all the directors present at the meeting.

(v) **Permission to BoD to delegate some of its powers [First Proviso to Section 179 (3)]:** The Board may, by a resolution passed at a meeting, delegate the powers specified in clauses (d) to (f) above (*i.e.* borrowing of monies, investing of funds and granting of loans or giving of guarantee or providing of security in respect of loans). The delegation may be made on such **conditions** as may be specified and to the following:

1. any committee of directors,
2. the managing director,
3. the manager or any other principal officer of the company, or
4. the principal officer of the branch office (if the company has a branch office).

(vi) **Imposing of restrictions and conditions by the shareholders [Section 179 (4)]:** The company through the general meeting has powers to impose restrictions and conditions on the exercise by the Board of any of the powers specified in Section 179.

In other words, shareholders of a company are very much in their right to impose restrictions and conditions on the powers of the Board of Directors. The shareholders may exercise the

powers of imposing restrictions by passing resolutions at the general meetings and may also make regulations (having only retrospective effect) curtailing the extent of powers exercisable by the Board.

As we know, the Board of Directors are fully empowered to manage day-to-day affairs of the company. The shareholders cannot impose their will on the Board; they cannot interfere and instruct the Board to discharge certain powers in a particular manner unless there are reasons to do so. In the following representative cases, however, the shareholders are empowered to exercise the powers of the Board:

- (a) **when directors are acting *malafide*** i.e. their conduct is such that they are acting for their own benefits at the expense of the interests of the company. Thus, when directors are wrong-doers and their personal interest conflicts with their duty towards the company, the majority shareholders shall take decisions to undo the wrong done by the directors.
- (b) **when all the directors are interested in a particular transaction** and therefore, incompetent to act due to absence of quorum. In such a case, shareholders shall decide through majority in the general meeting whether to entertain that transaction or not.
- (c) **when there happens to be deadlock in the management** because the directors are not on talking terms or unwilling to act; thus, paving way for the shareholders to ensure running of the company
- (vii) **Exemption to banking companies [Second Proviso to Section 179 (3)]**: In respect of banking companies following exemptions are provided:
 - (a) **the acceptance of deposits of money by a banking company in the ordinary course of its business from the public** which is repayable on demand or otherwise and withdrawable by cheque, draft, order or otherwise shall not be deemed to be a borrowing of monies within the meaning of Section 179;
 - (b) further, **the placing of monies on deposit by a banking company with another banking company on such conditions as the Board may prescribe** shall not be deemed to be a making of loans by a banking company within the meaning of Section 179.

Note: By way of Explanation I, it is clarified that clause (d) above (i.e. to borrow monies) shall not apply to borrowings by a banking company from other banking companies or from the Reserve Bank of India, the State Bank of India or any other banks established by or under any Act. Thus, in such cases of borrowings by a banking company, there is no need to obtain sanction by means of a resolution passed at a duly convened Board meeting. This is practical also to provide such exemption, keeping in view the business of a banking company.



8. RESTRICTIONS ON POWERS OF BOARD [SECTION 180]

The powers of the Board of Directors of a company are not unrestricted or uncontrollable as Section 180 portrays. This Section contains directive provisions which direct that the powers in respect of specified matters shall be exercised by the Board subject to the certain restrictions *i.e.* in such cases the exercise of powers by the Board shall be restricted as per law. Section 180 is not applicable to a private company.

(i) **Matters in respect of which powers shall be exercised after obtaining consent by a special resolution:** According to Section 180 (1), following are the matters in respect of which the Board shall exercise the powers with the consent of the company by a **special resolution** and not on its own simply by passing a Board resolution at a Board meeting:

(a) To **sell, lease or otherwise dispose of the whole or substantially the whole of the undertaking of the company** or where the company owns more than one undertaking, of the whole or substantially the whole of any of such undertakings. In other words, out of multiple undertakings of a company even if one is sold, leased or disposed of, either wholly or substantially, the consent by special resolution shall be required.

Imposition of conditions by the shareholders: According to Section 180 (4), any special resolution passed by the company consenting to the transaction of sell, lease, etc., may stipulate certain conditions and if so, the same need to be specified in such resolution. Among others, the conditions shall be regarding the use, disposal or investment of the sale proceeds which may result from the transactions.

Section 180 (4) not to be taken as authorization for reduction in capital: It is provided that sub section (4) shall not be deemed to authorise the company to effect any reduction in its capital. Such reduction must be effected in accordance with the provisions contained in the Companies Act, 2013.

No need for special resolution if selling, leasing, etc. is part of ordinary business of the company: According to Section 180 (3) (b), the restriction in the form of special resolution is not attracted to the sale or lease of any property of the company where its ordinary business consists of such selling or leasing.

Clean title of the buyer, etc. [Section 180 (3) (a)]: In respect of a buyer who buys or in respect of other person who takes on lease (*i.e.* lessee) any property, investment or undertaking as is referred to in Section 180 (1) (a) in **good faith**, his title shall not be affected despite the fact that the directors resorted to selling or leasing without first obtaining the consent of the company by a special resolution.

Note 1: The expression “**undertaking**” means an undertaking in which the investment of the company **exceeds twenty per cent** of its **net worth**¹⁰ as per the audited balance sheet of the preceding financial year or an undertaking which generates **twenty per cent** of the total income of the company during the previous financial year.

Note 2: The expression “**substantially the whole of the undertaking**” in any financial year shall mean **twenty per cent or more** of the value of the undertaking as per the audited balance sheet of the preceding financial year.

Note 3: In case the provisions of Section 110 of the Act apply to the company which is resorting to sale of the whole or substantially the whole of its undertaking in terms of Section 180 (1) (c), it shall pass the special resolution containing such item of business by means of voting through postal ballot. [Refer Rule 16 (i) of the Companies (Management and Administration) Rules, 2014.]

Note 4: A One Person Company and other companies having members up to two hundred are not required to transact any business through postal ballot.[refer Proviso to Rule 16 of the Companies (Management and Administration) Rules, 2014.]

- (b) To **invest otherwise in trust securities** the amount of compensation received by it as a result of any merger or amalgamation. It implies that if the investment of the compensation amount is made in trust securities¹¹, there is no need to obtain consent of the members through a special resolution.
- (c) To **borrow money**, where the money to be borrowed, together with the money already borrowed by the company will exceed aggregate of its paid-up share capital, free reserves¹² and securities premium apart from temporary loans obtained from the company's bankers in the ordinary course of business.

¹⁰ 'Net worth', according to Section 2 (57) of the Act means 'the aggregate value of the paid-up share capital and all reserves created out of the profits and securities premium account, after deducting the aggregate value of the accumulated losses, deferred expenditure and miscellaneous expenditure not written off, as per the audited balance sheet, but does not include reserves created out of revaluation of assets, write-back of depreciation and amalgamation'.

¹¹ 'Trust securities' are mentioned in Section 20 of the Indian Trust Act, 1882.

¹² 'Free reserves' according to Section 2 (43) of the Act means 'such reserves which, as per the latest audited balance sheet of a company, are available for distribution as dividend:

Provided that—

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

In simple words, '**borrowings**' (including loans raised for meeting financial expenditure of a capital nature) are not to include temporary loans which are obtained by the company from its bankers in the ordinary course of business.

Limit on 'borrowings' need to be specified: Section 180 (2) requires that every special resolution passed by the company in general meeting in relation to the 'borrowings' shall specify the **total amount** up to which monies may be borrowed by the Board of Directors. Thus, the Board cannot be given blanket powers to borrow monies up to any extent of its choice, but the special resolution must specify the total amount that can be borrowed. In other words, a rational thinking in the form of specifying a 'particular amount' must be exercised by the shareholders so that borrowings are restricted. The specifying of total amount that can be borrowed is a step in this direction. Excessive borrowings at the whims and caprices of the Board are dangerous to the company as a whole including its shareholders.

Debt raised in excess of the specified limit [Section 180 (5)]: If a company incurs debt in excess of the limit imposed i.e. more than the 'total amount' specified in the special resolution, it shall not be valid or effectual from the point of view of lender unless such lender proves that he advanced the loan in good faith and without knowledge that the limit imposed had been exceeded. Thus, lender has to be fully cautious before extending any loan to a company. The loaned amount must not be in excess of the limit imposed otherwise it shall not be legally enforceable against the company. In other words, the lender must be aware in no uncertain terms the implications of Section 180 (5) and must carefully check the financial statements as well as the special resolution, if any, passed by the company before extending any loan facility to it.

Meaning of "Temporary Loans": It is clarified by way of *Explanation* that the term '**temporary loans**' means loans repayable on **demand or within six months** from the date of the loan such as short-term, cash credit arrangements, the discounting of bills and the issue of other short-term loans of a seasonal character, but does not include loans raised for the purpose of financial expenditure of a capital nature.

Exemption to a banking company: The acceptance by a banking company, in the ordinary course of its business, of deposits of money from the public, repayable on demand or otherwise, and withdrawal by cheque, draft, order or otherwise, shall **not** be deemed to be a **borrowing of monies** by the banking company.

- (d) To **remit, or give time for the repayment of, any debt due from a director**. Thus, if any debt is repayable by a director, then it cannot be remitted or its repayment time cannot be extended unless consent by passing a special resolution is given by the company.

- (ii) **Contribution to *bona-fide* and charitable funds, etc.:** This type of contributions by a company beyond certain limit requires passing of an ordinary resolution as required by Section 181, the provisions of which are discussed later in the Chapter.

Example 7: The Board of Directors of Stepping Stones Publications Ltd. resolved to borrow a sum of ₹ 15 crore from a nationalized bank at a Board meeting held on 15.1.2019. One of the directors, who opposed the said borrowing as not in the interest of the company has raised an issue that the said borrowing is outside the borrowing powers of the Board. The following data is given for your information:

- (i) Share Capital ₹ 5 crore
- (ii) Reserves and Surplus ₹ 5 crore
- (iii) Secured Loans ₹ 15 crore
- (iv) Unsecured Loans ₹ 5 crore

According to the provisions of Section 180(1)(c) of the Companies Act, 2013, , the borrowings should not exceed the aggregate of the paid-up share capital, free reserves and securities premium. While calculating the limit, the temporary loans obtained by the company from its bankers in the ordinary course of business will be excluded. However, from the figures available in the present case, the proposed borrowing of ₹ 15 crore will exceed the limit calculated as per the given information. Thus, the proposed borrowings are beyond the powers of the Board of directors.

In view of the above position, the management of Stepping Stone Publications Ltd., should take steps to pass a special resolution authorising to borrow the proposed amount of ₹ 15.00 crore, so that the requirement of Section 180(1)(c) is satisfied. Only thereafter, the proposed borrowing can be availed of.

Exemption

*As notified by the MCA, Section 180 of the Act (i.e. restrictions on the powers of the Board) shall not apply to a **private company** which has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar. [Notification No. 464(E), dated 5th June, 2015 as amended by Notification No. 583 (E), dated 13th June, 2017.]*

1. In an order passed by the National Company Law Appellate Tribunal, New Delhi, *Priyaranjani Fibres Ltd. v. D. Srinivasa Rao* , it was laid that where director of company entered into an agreement with outsider to sell shares of himself and others without prior approval of shareholders, said agreement would not be binding on shareholders.

In the given case, D1, director of company entered into an agreement with appellant, who was an outsider, to sell shares of himself and respondent shareholders to appellant and let management of company go in hands of appellant. However, there was nothing to show that there was any shareholders' meeting on decision to permit one of director i.e. D1 to part with management of

company to outsider. Further, company was a sick company and there could not be change of management without permission of BIFR. However, there was nothing to show that any such consent were sought and granted. further, said agreement was an agreement between D1 and appellant and there was nothing to show that respondent shareholders were party to such agreement or that company was party to such agreement. Thus it was held that, said agreement would not be binding on respondent shareholders and company.

2. National Company Law Tribunal, Chennai Bench laid down in *Smt. Sulochana v. Arunodhaya Enterprises Ltd.* that as per Section 180 of the Companies Act, 2013, Articles of association of a company authorised managing director to carry on management of affairs of company. Board of directors of company had not restrained managing director from performing any particular act or function in management of business of company. Therefore, it could be safely concluded that managing director was empowered to sell property, particularly when company itself was in business of real estate and for every genuine sale transaction managing director need not obtain permission of shareholders.



9. COMPANY TO CONTRIBUTE TO BONA FIDE AND CHARITABLE FUNDS, ETC. [SECTION 181]

Section 181 of the Act, applicable to both public and private companies, empowers the Board of Directors to contribute to *bona fide* charitable and other funds up to a particular limit which if exceeded needs to be permitted by company through passing an ordinary resolution.

Limit on contribution by the Board of Directors: The Board is empowered to contribute any amount in any financial year if the aggregate amount of such contribution does not exceed five per cent of the average net profits of the company for the three immediately preceding financial years.

Where the above limit is exceeded: In case the aggregate contribution amount in any financial year is beyond the limit specified for the Board, prior permission of the company in general meeting shall be required for such contribution.

The expression “other funds” is wide enough to enable contributions of the kind, specified in the special resolution to be made by the company. [*Straw Products Ltd. vs. Registrar of Companies* [1969].

Example 8: The Board of Directors of Very Well Ltd., is contributing every year to a charitable organization a sum of ₹ 60, 000. In a particular year, the company suffered losses and the directors are contemplating to contribute the said amount in spite of the losses.

Under section 181 of the Companies Act, 2013, the Board of Directors of a company is authorized to contribute to *bonafide* charitable and other funds. However, in case the aggregate amount of such contribution in any financial year exceeds five per cent. of its average net profits for the three

immediately preceding financial years, prior permission of the company in general meeting shall be required.

The section does not make it mandatory for the company to have a profit for making a charitable contribution in any financial year. As the amount of donation is restricted to the average of immediately previous 3 years' profits, it is possible for a company suffering a loss to make contribution provided it is made to a *bonafide* charitable fund and the average of the three immediately preceding financial years' profits (including current losses) is positive.

In the present case, even though the company has incurred a loss it can contribute to the charitable fund only if it is a *bonafide* charitable fund and the amount is up to 5% of the average of the immediately preceding three years' profits (including current losses). In case the contribution exceeds the limit, the prior approval of the members must be taken at a general meeting of the company.



10. PROHIBITIONS AND RESTRICTIONS REGARDING POLITICAL CONTRIBUTIONS [SECTION 182]

Section 182 of the Act, deals with the provisions relating to prohibitions and restrictions regarding political contributions. These provisions are stated as under:

- (i) **Contribution by a company to political parties:** A company is permitted to contribute any amount (without any limit) directly or indirectly to any political party, notwithstanding anything contained in any other provision of the Companies Act, 2013. It is to be noted that Section 182 (1) has overriding effect.

*Meaning of Political Party*¹³: The term "political party" means a political party registered under section 29A of the Representation of the People Act, 1951.

- (ii) **Companies not allowed contributing to political parties:** The following companies are not allowed to contribute to any political party:
 - (a) a Government company; and
 - (b) a company which has been in existence for less than three financial years.
- (iii) **Procedure for making contribution:** A company shall make the contribution to a political party only after a resolution authorising the making of such contribution is passed at a meeting of the Board of Directors. In effect, such resolution shall be deemed to be justification in law for the making of the contribution authorised by it. [Proviso to Section 182(1)]

¹³ As per Explanation to Section 182.

- (iv) **Deemed political contributions [Section 182(2)]:** In addition to making any direct contribution to a political party, **following contributions** are also deemed as political contributions:
- (a) a **donation or subscription or payment** given by a company to a person who, to its knowledge, is carrying on any activity which, at the time at which such donation or subscription or payment was given, can reasonably be regarded as **likely to affect public support for a political party**;
 - (b) the **amount of expenditure** incurred, directly or indirectly, by a company **on an advertisement in any publication** being in the nature of a souvenir, brochure, tract, pamphlet or the like:
 - (1) where such publication is by or on behalf of a political party; and
 - (2) where such publication is not by or on behalf of, but for the advantage of a political party.
- (v) **Disclosure of contributed amount [Section 182(3)]:** Every company shall disclose in its profit and loss account the total amount contributed by it under Section 182 during the financial year to which the account relates.
- (vi) **Modes of contribution [Section 182 (3A)]:** The contribution to a political party under Section 182 shall be made according to following **modes**:
- by an account payee cheque drawn on a bank; or
 - by an account payee bank draft; or
 - by using electronic clearing system through a bank account; or
 - through any instrument, issued pursuant to any scheme¹⁴ notified under any law for the time being in force, for contribution to the political parties.[Section 182(3A)]
- (vii) **Punishment for contravention:** If a company makes any contribution in contravention of the provisions of Section 182, the punishment shall be as under:
- **Company:** punishable with fine up to **five times** the amount of contribution so made.
 - **Every defaulting officer:** punishable with imprisonment up to **six months** and with fine up to **five times** the amount of contribution so made.

¹⁴ A scheme relating to 'Electoral Trust Companies' has come into force in terms of Section 2 (22AA) of the Income-tax Act, 1961 read with Ministry of Finance Notification No. S.O. 309 (E), dated 31-01-2013.

The MCA vide General Circular 19/ 2013 dated 10th December 2013, issued a clarification on disclosures to be made under Section 182 (3) while making **contributions to 'Electoral Trust'**. According to the Circular:

With the coming into force of the scheme relating to 'Electoral Trust Companies' under Section 2 (22AA) the Income Tax Act, 1961 read with Ministry of Finance Notification No. S.O. 309(E) dated 31st January, 2013, it will be expedient to explain the requirements of disclosure on part of a company of any amount or amounts contributed by it to any political parties under Section 182(3) of the Companies Act, 2013.

The Ministry hereby clarifies that:

- (i) Companies contributing any amount or amounts to an 'Electoral Trust Company' for contributing to a political party or parties are not required to make disclosures required under Section 182(3) of Companies Act 2013. It will suffice if the Accounts of the company disclose the amount released to an Electoral Trust Company.
- (ii) Companies contributing any amount or amounts directly to a political party or parties will be required to make the disclosures laid down in Section 182(3) of the Companies Act, 2013.
- (iii) Electoral trust companies will be required to disclose all amounts received by them from other companies/sources in their Books of Accounts and also disclose the amount or amounts contributed by them to a political party or parties as required by Section 182(3) of Companies Act, 2013.

Example 9: The Board of Directors of LM Ltd., incorporated in April, 2017, proposes to donate ₹ 50,000 to a political party for the F.Y. 2019-20. The average net profits determined in accordance with the provisions of the Companies Act, 2013 during the two immediately preceding financial years are ₹ 20,00,000. As per section 182(1) of the Companies Act, 2013 any company may contribute any amount directly or indirectly to any political party except a government company and a company which has been in existence for less than three financial years.

However in the given case, as LM Ltd. happens to be a company which has been in existence for less than three financial years. Hence, it is not permitted to donate any amount to the concerned political party for the F.Y. 2019-20.

Example 10: Sea Hawk Cycles Limited is a company incorporated four years ago. It has earned profits amounting to ₹ 5 lakhs, ₹ 8 lakhs and ₹ 11 lakhs respectively during the last three financial years. The Board of Directors of the company proposes to donate a sum of ₹ 50,000 to a political party. In view of the section 182(1), Sea Hawk Cycles Limited can contribute the said amount of ₹ 50,000 to the concerned political party. However, it needs to pass a board resolution authorising making of such contribution at a meeting of the Board of Directors.



11. POWER OF BOARD AND OTHER PERSONS TO MAKE CONTRIBUTIONS TO NATIONAL DEFENCE FUND, ETC. [SECTION 183]

Section 183 of the Act, empowers the Board and other authorised persons to make contributions to the National Defence Fund, etc. as described below:

- (i) **Contribution of amount to National Defence Fund/other fund as approved by the Central Government:**
 - (a) **No limit:** Contribution to the National Defence Fund or any other Fund approved by the Central Government for the purpose of national defence can be made without any limit.
 - (b) **Exercise of power:** The power to make such contribution shall be exercised by:
 - The Board of Directors of the company; or
 - Any person or authority exercising the powers of the Board of Directors or of the company in general meeting.
 - (c) **Overriding effect:** Section 183 has overriding effect *i.e.* the contribution may be made notwithstanding anything contained in Sections 180, 181 and 182 or any other provision of the Companies Act, 2013 or in the memorandum, articles or any other instrument relating to the company.
- (ii) **Disclosure in profits and loss account:** Every company shall disclose in its profits and loss account the total amount or amounts contributed by it to the National Defence Fund or any other approved fund, during the financial year to which the amount relates.



12. DISCLOSURE OF INTEREST BY DIRECTOR [SECTION 184]

The office of director in a company is that of 'trust'. A person holds the directorship in a fiduciary capacity. As trustee of the assets of the company, the director is duty bound to pass on the benefits accruing from all such transactions which belong to the company. At any stage if he becomes interested in a transaction the benefits of which rightfully accrue to the company, he must disclose his interest so that the Board and if required, the company, may take a rational decision whether to continue with that transaction or not. The disclosure of interest to be made by a director includes both 'general disclosure of interest' and 'specific disclosure of interest'. Section 184 of the Act, which contains provisions in respect of 'disclosure of interest' by the directors, is applicable to all the companies and their directors. These provisions are discussed as under:

- (i) **General disclosure of interest [Section 184(1)]:** Every director shall disclose his concern or interest in any company or companies or bodies corporate, firms, or other association of

individuals which shall include the shareholding, in the manner prescribed in Rule 9 of the Companies (Meetings of Board and its Powers) Rules, 2014. The intention of law behind such disclosure is to make known the other directors of the company about the interest of concerned director in other companies, firms, etc.

When to make general disclosure of interest: Every director shall disclose his interest:

- (a) at the first meeting of the Board in which he participates as a director, and
- (b) thereafter, at the first meeting of the Board in every financial year, or
- (c) whenever there is any change in the disclosures already made, then at the first Board meeting held after such change.

Provisions of Rule 9: As regards **manner of disclosure** and certain other matters, the provisions of Rule 9 are given as under:

Every director shall disclose his concern / interest	• by written notice
in Form	• MBP-1.
Such Director shall	• cause it to be disclosed at the meeting held immediately after the date of the notice
All notices shall be kept	• at the registered office of the company.
Preserved	• for eight years from the end of the financial year to which they relate.
They shall be kept in the custody of the	• Company Secretary or any other person authorised by the Board

(ii) **Specific disclosure of interest:** According to Section 184 (2), a director of a company shall make a specific disclosure of interest whenever he, in any way, whether directly or indirectly, is concerned or interested in a contract or arrangement or proposed contract or arrangement entered into or to be entered into:

- (a) with a body corporate in which such director or such director in association with any other director holds **more than two per cent shareholding** of that body corporate; or
- (b) with a body corporate in which such director is a promoter, manager, Chief Executive Officer; or
- (c) with a firm or other entity in which, such director is a partner, owner or member.

When to make specific disclosure of interest: The disclosure shall be made as under:

- The interested director shall disclose the nature of his concern or interest at the meeting of the Board in which the contract or arrangement is discussed for the first time; and
- He shall not participate in such meeting. 'Non-participation' implies that he shall not discuss the matter relating to such contract and also shall not vote if there happens to be a voting in this connection.
- It may happen that any director is not so concerned or interested at the time of entering into such contract or arrangement. However, if he becomes interested after the contract or arrangement is entered into, he shall disclose his concern or interest forthwith when he becomes so or at the first meeting of the Board held after his becoming concerned or interested.

Exception/Modification

1. In case of a **private company** which has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar, the provisions of Section 184 (2) shall apply with the exception that the interested director may participate in such meeting after disclosure of his interest. [Notification No. G.S.R. 464(E), dated 5th June, 2015 as amended by Notification No. G.S.R. 583 (E), dated 13th June, 2017.]

2. In respect of a **Section 8 company** which has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar, the provisions of Section 184(2) shall apply only if the transaction with reference to Section 188 on the basis of terms and conditions of the contract or arrangement **exceeds one lakh rupees**. [Notification No. G.S.R. 466(E), dated 5th June 2015 as amended by Notification No. G.S.R. 584 (E), dated 13th June, 2017.]

(iii) **Contract voidable at the option of company if there is non-disclosure [Section 184(3)]:**

A contract or arrangement entered into by the company shall be voidable at its option if the interested director who has a direct or indirect concern or interest in such contract or arrangement, does not disclose his interest as required by Section 184 (2) or if such director participates in the meeting where such contract or arrangement is discussed.

It may be noted that the contract is voidable and not void and the option of rescinding the contract lies with the company and not with the interested director. Thus, if the company decides to honour the contract, the interested director cannot rescind it because of irregularity.

(iv) **Punishment for contravention [Section 184(4)]:** If a director of the company contravenes the provisions of Section 184 (1) and (2) i.e. does not disclose his interest or furnishes wrong information in this respect, he shall be liable to a penalty of one lakh rupees.

- (v) **No restriction on directors:** Nothing in Section 184 shall be taken to prejudice the operation of any rule of law restricting a director of a company from having any concern or interest in any contract or arrangement with the company.
- (vi) **Exemption from disclosure if the holding is up to two per cent:** According to Section 184 (5) (b), the provisions of Section 184 regarding disclosure by interested director shall not apply to any contract or arrangement entered into or to be entered into between two companies where any of the directors of the either company or two or more of them together holds or hold **not more than 2%** of the paid-up share capital in the other company.

Example 11: Y Ltd. entered into a contract with Z Ltd. which has a paid-up capital of ₹50 lakhs. One of the directors of Y Ltd. is holding equity shares of the nominal value of ₹ 50,000 in Z Ltd. but he did not disclose his interest at the appropriate Board meeting.

In this case, as per section 184 (2) of the Companies Act, 2013 the disclosure of interest by directors is not required in any contract or arrangement between two companies where any of the directors of the company or two or more of them together holds or hold not more than 2% of the paid-up share capital in the other company. Here, the holding of the director of Y Ltd. in Z Ltd. is only 1% [*i.e.* $(50,000/50,00,000) \times 100 = 1\%$] which is less than 2%. Therefore, he is does not require to disclose his interest regarding holding of equity shares in Z Ltd.



13. DEFECTS IN APPOINTMENT OF DIRECTORS NOT TO INVALIDATE ACTIONS TAKEN [SECTION 176]

Section 176 of the Act contains protective provisions by which actions taken by a director shall not get invalidated if subsequently it is noticed that there happened to be defects in his appointment. The validation of actions provides a kind of protection to the company as well as the third parties. The provisions of Section 176 are stated as under:

- (i) **No act done by a person as a director shall be deemed to be invalid**, if it was subsequently noticed that his appointment was invalid by reason of:
- any defect; or
 - disqualification; or
 - had been terminated by virtue of any provision contained in the Companies Act, 2013 or in the articles of the company.
- (ii) **Acts not valid if done after noticing his appointment to be invalid or to have terminated:** It is provided that Section 176 shall not be deemed to give validity to any act done by the director after his appointment has been noticed by the company to be invalid or to have terminated.

In other words, any subsequent act done by a director shall not get validated under the following circumstances:

where it comes to the notice of the company that his appointment is invalid or illegal or there is no appointment.

where it is in the notice of the company that his appointment has been terminated.

where it is noticed by the company that his acts are illegal i.e. ultra vires the company or the Companies Act.

where it was well within the knowledge of the third party that the appointment of director was not valid or there existed any irregularity or there was any disqualification attached to the director and still such party dealt with him.

where the director knows it fully that his term of office has expired but he continues to occupy his office despite such knowledge.

where a person exercises his powers as director though he apparently knows that he has no authority to exercise such powers because his appointment was invalid or he has since been terminated.

- (iii) **Protection to the acts of MD or WTD or Manager:** In terms of Section 196 (5), any act done by a managing director or whole-time director or manager before his appointment was disapproved by the company at a general meeting shall be deemed to be valid.

Example 12: Mr. Mohan was appointed as director at the Annual General Meeting of a company held on 30th September, 2018 and he functioned in the capacity as director from then onwards. Subsequently, during the mid of August, 2019, it was noticed that there were certain irregularities in his appointment and therefore, on 31st August, 2019, his appointment was declared invalid. However, Mr. Mohan continued to act as director even after 31st August, 2019.

In the given **example**, in view of the Section 176, the acts done by Mr. Mohan till the date of noticing irregularity in his appointment shall be deemed as valid and binding on the company.

Any act done by him after the date on which irregularity in his appointment was noticed by the company shall be invalid. Accordingly, acts done by Mr. Mohan after 31st August, 2019 shall be invalid and not binding upon the company.

High Court of Andhra Pradesh in *Smt. Dr. Renuka Datla v. Biological E Ltd.* laid that benefit of section 176 of the Companies Act, 2013, is generally available to third parties who enter into transactions with a company not knowing what internal structure and mechanism of company is. It was mentioned that a person such as a Managing Director or a Director who is expected to know what is right and what is wrong and what is legal and what is illegal, cannot be allowed to presume things in his favour, and if at end he fails to prove that he has acted as per law, he cannot take shelter under section 176, more so, in a case where Directors usurped their office.



14. LOAN TO DIRECTORS, ETC. [SECTION 185]

Section 185 of the Act contains provisions which impose restrictions on the loans, etc. being given to directors, etc. These provisions are stated below:

- (i) **Imposition of restrictions [Section 185 (1)]:** A company (subject to exemptions stated in the Box given later) is not permitted, directly or indirectly, to advance any loan, including any loan represented by a book debt to, or to give any guarantee or provide any security in connection with any loan taken by,—
 - (a) any director of company, or of a company which is its holding company or any partner or relative of any such director; or
 - (b) any firm in which any such director or relative is a partner.
- (ii) **Relaxation from restrictions [Section 185 (2)]:** Subject to the specified conditions, a company is permitted to:
 - advance any loan including any loan represented by a book debt, or
 - give any guarantee or provide any security in connection with any loan taken,
 by any person in whom any of the director of the company is interested.

The specified conditions to be followed are:

- (a) a **special resolution** is passed by the company in general meeting.

However, the explanatory statement to the notice for the relevant general meeting shall disclose;

- the *full particulars* of the loans given or guarantee given or security provided; and
- the *purpose* for which the loan or guarantee or security is proposed to be utilized by the recipient of the loan or guarantee or security and

- any other relevant fact;
- (b) the loans are utilized by the **borrowing company** for its **principal business activities**.

Explanation: The expression "any person in whom any of the director of the company is interested" means—

- (a) any **private company** of which any such director is a director or member;
 - (b) any **body corporate** at a general meeting of which **not less than twenty-five per cent** of the total voting power may be exercised or controlled by any such director, or by two or more such directors, together; or
 - (c) any **body corporate**, the Board of directors, managing director or manager, whereof is accustomed to act in accordance with the directions or instructions of the Board, or of any director or directors, of the lending company.
- (iii) **Non-applicability of restrictions [Section 185 (3)]:** In the following cases, restrictions stated in Section 185 (1) or specified conditions for relaxation of restrictions stated in Section 185 (2) shall not apply:
- (a) where any loan is given to a **managing or whole-time director**—
 - (i) as a part of the conditions of service extended by the company to all its employees; or
 - (ii) pursuant to any such **scheme** which is approved by the members by a **special resolution**.
 - (b) where a company in the ordinary course of its business:
 - provides loans or gives guarantees or securities for the due repayment of any loan; and
 - in respect of such loans an **interest is charged at a rate not less than the rate of prevailing yield** of one year, three years, five years or ten years Government security closest to the tenor of the loan.
 - (c) (i) where any loan is made by a holding company to its wholly owned subsidiary company; or
 - (ii) where any guarantee is given or security is provided by a holding company in respect of any loan made to its wholly owned subsidiary company.
 - (d) where any guarantee is given or security is provided by a holding company in respect of loan made by any bank or financial institution to its subsidiary company.

As a pre-condition, it must be ensured that the loans made under clauses (c) and (d) are utilized by the subsidiary company for its principal business activities.

- (iv) **Penalty for contravention:** Penalty for contravention of the provisions of Section 185 (i.e. if any loan is advanced or a guarantee or security is given or utilized contravening the provisions of Section 185) shall be as under:
- Company:** punishable with minimum fine of ₹ 5,00,000 and maximum fine of ₹ 25,00,000.
 - Every defaulting officer:** punishable with imprisonment up to six months or with minimum fine of ₹ 5,00,000 and maximum fine of ₹ 25,00,000.
 - the director or the other person to whom any loan is advanced or guarantee or security is given in connection with any loan taken by him or the other person: punishable with imprisonment up to six months or with minimum fine of ₹ 5,00,000 and maximum fine of ₹ 25,00,000, or with both.

Exemptions

1. Section 185 shall not apply to **Government company** in case such company obtains approval of the Ministry or Department of the Central Government which is administratively in charge of the company, or, as the case may be, the State Government before making any loan or giving any guarantee or providing any security under the section.

Note: The above exemption is applicable to a Government company if it has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar.

[Notification No. G.S.R. 463(E), dated 5th June 2015 as amended by Notification No. G.S.R. 582 (E), dated 13th June 2017.]

2. Section 185 shall not apply to a **private company-**

- In whose share capital no other body corporate has invested any money;
- If the borrowings of such a company from banks or financial institutions or anybody- corporate is less than twice of its paid-up share capital or fifty crore rupees, whichever is lower, and
- Such company has no default in repayment of such borrowings subsisting at the time of making transactions under this section.

Note: The above exemption is applicable to a private company if it has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar.

[Notification No. G.S.R 464(E), dated 5th June 2015 as amended by Notification No. G.S.R 583(E), dated 13th June 2017.]

3. Section 185 shall not apply to the **Nidhis**, provided the loan is given to a director or his relative in their capacity as members and such transaction is disclosed in the annual accounts by a note. However, while complying with such exception, the Nidhis shall ensure that the interests of their shareholders are protected.

[Notification no. G.S.R. 465(E), dated 5th June 2015.]



15. LOAN AND INVESTMENT BY COMPANY [SECTION 186]

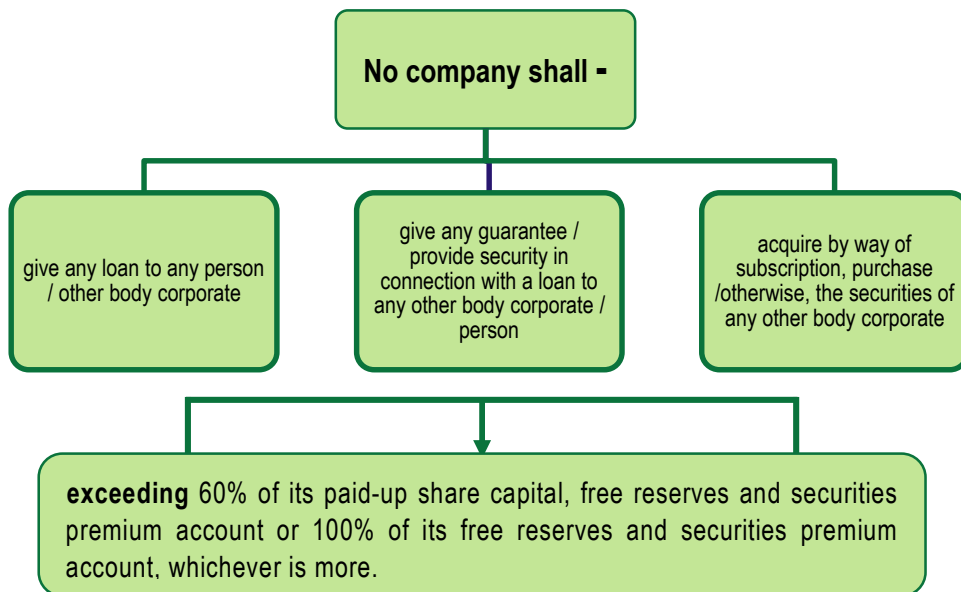
Section 186 of the Act, applicable to both public and private companies, deals with the provisions relating to 'Loan and Investment' by a company. In addition, Rules 11, 12 and 13 also contain provisions governing the making of loans and investments, giving of guarantees and providing of securities by a company. These provisions are discussed as under:

- (i) **Investment permitted through two layers of Investment Companies [Section 186(1)]:** A company, unless otherwise prescribed, is not permitted to make investment through more than two layers of investment companies. Placing of such a restriction helps in preventing diversion of funds. It is a common experience that the funds can be more flagrantly diverted if a company invests through a number of step-down subsidiaries.

Note: It is clarified by way of *clause (a) of Explanation* that the expression “**investment company**” means a company whose principal business is the acquisition of shares, debentures or other securities. Further, a company will be deemed to be principally engaged in the business of acquisition of shares, debentures or other securities, if its **assets** in the form of investment in shares, debentures or other securities constitute **not less than fifty per cent** of its total assets, or if its **income** derived from investment business constitutes **not less than fifty per cent** as a proportion of its gross income.

Exception to the rule of two layers: In the following cases, the provisions of Section 186 (1) shall not apply *i.e.* rule of 'two layers' shall not be applicable:

- (a) **Acquisition of a company incorporated outside India:** If a company acquires any other company incorporated in a country outside India and if such other company has investment subsidiaries beyond two layers as per the laws of such country, the rule of 'two layers' shall not prevent this kind of acquisition.
 - (b) **Subsidiary from having an investment subsidiary:** Again, the rule of 'two layers' shall not prevent a subsidiary company from having any investment subsidiary for the purposes of meeting the requirements under any law or under any rule or regulation framed under any law for the time being in force.
- (ii) **Imposition of limit on the quantum of loan and investment made by a company:** According to Section 186 (2), following types of transactions (both direct and indirect) shall be subject to the specified limit as depicted in the diagram:
- (a) giving of **loan** to any person or other body corporate;
 - (b) giving of **guarantee** or provision of **security** in connection with a loan to any other body corporate or person;
 - (c) acquiring by way of subscription, purchase or otherwise the securities of any other body corporate.



Explanation: For the purposes of Section 186 (2), the word "person" does not include any individual who is in the employment of the company.

Loans and Advances to Employees – Clarification on the applicability of Section 186

*The MCA has clarified that loans and/or advances made by the companies to their employees, other than the managing or whole-time directors (which is governed by Section 185) are **not** governed by the requirements of Section 186.*

This clarification will, however, be applicable if such loans/advances to employees are in accordance with the conditions of service applicable to employees and are also in accordance with the remuneration policy, in cases where such policy is required to be formulated.

[General Circular No. 04/2015, dated 10/3/2015.]

In other words, a company is permitted to enter into transactions of giving loan or guarantee or providing security or acquiring of securities (i.e. shares, debentures, etc.), in the aggregate, upto 60% of its paid-up share capital (both equity and preference), free reserves and securities premium or 100% of its free reserves and securities premium, whichever is more.

- (iii) **Prior approval by a special resolution for exceeding limit [Section 186(3)]:** Where the aggregate of the loans and investment so far made, the amount for which guarantee or security so far provided to or in all other bodies corporate along with the investment, loan, guarantee or security proposed to be made or given by the Board, exceed the limits specified under Section 186 (2), no investment or loan shall be made or guarantee shall be given or security shall be provided unless previously authorised by a special resolution passed in a general meeting.

Note 1: In case the provisions of Section 110 of the Act apply to the company which is considering giving of loans or extending guarantee or providing security in excess of the limit specified under Section 186 (3), it shall pass the special resolution containing such item of business by means of voting through postal ballot. [refer Rule 16 (j) of the Companies (Management and Administration) Rules, 2014.]

Note 2: A One Person Company and other companies having members up to two hundred are not required to transact any business through postal ballot. [refer Proviso to Rule 16 of the Companies (Management and Administration) Rules, 2014.]

Disclosure of total amount in resolution in respect of loan or guarantee or security or acquisition: As per the Rule 13 of the Companies (Meetings of Board and its Powers) Rules, 2014, a resolution passed at a general meeting in terms of Section 186 (3) to give any loan or guarantee or investment or providing any security or the acquisition under Section 186 (2) shall specify the total amount up to which the Board of Directors are authorised to give such loan or guarantee, to provide such security or make such acquisition.

Exemption from special resolution [First Proviso to Section 186 (3) and Rule 11 (1)]: However, where a loan or guarantee is given or where a security has been provided by a company to its wholly owned subsidiary company or a joint venture company, or acquisition is made by a holding company, by way of subscription, purchase or otherwise of, the securities of its wholly owned subsidiary company, the requirement of passing a special resolution as required by Section 186 (3) shall not apply.

Disclosure in financial statement [Second Proviso to Section 186 (3) and Proviso to Rule 11 (1)]: In case of exemption from special resolution, the company shall disclose the details of such loans or guarantee or security or acquisition in the financial statement as provided under Section 186 (4).

- (iv) **Disclosure to members [Section 186(4) and Proviso to Rule 13]:** The company shall make full disclosure to the members as depicted in the following diagram:

Company shall disclose to the members in the financial statements the full particulars of-		
loan given,	investment made or guarantee given or security provided,	the purpose for which the loan or guarantee or security is proposed to be utilized by the recipient of the loan or guarantee or security.

- (v) **Unanimous resolution of the Board [Section 186(5)]:**
- Any investment shall be made or loan or guarantee or security given by the company only after when the resolution sanctioning it is passed at a meeting of the Board **with the consent of all the directors present** at the meeting.

- The prior approval of the public financial institution concerned where any term loan is subsisting shall also be obtained.

Circumstances when no prior approval of public financial institution (PFI) is required [Proviso to Section 186 (5)]: Prior approval of a public financial institution (PFI) shall not be required where the aggregate of the loans and investments so far made, the amount for which guarantee or security so far provided to or in all other bodies corporate, along with the investments, loans, guarantee or security proposed to be made or given:

- does not exceed the limit as specified in section 186(2) (i.e. 60% of its paid-up share capital, free reserves and securities premium account or 100% of its free reserves and securities premium account, whichever is more), and
- there is no default in repayment of loan installments or payment of interest thereon as per the terms and conditions of such loan to the public financial institution.

- (vi) **Rate of interest on loan [Section 186 (7)]:** A loan under this section shall be given at a rate of interest which is not lower than the prevailing yield of one year, 3 year, 5 year or 10 year Government Security closest to the tenor of the loan.

1. Clarification in respect of Section 186 (7) - Rate of Interest

The MCA has clarified that in cases where effective yield (effective rate of return) on tax free bonds is greater than the prevailing yield of one year, three year, five year or ten year Government Security closest to the tenor of the loan, there is no violation of sub-section (7) of Section 186 of the Companies Act, 2013. [General Circular No. 06/2015, dated 9th April, 2015]

2. Modification in Section 186 (7) in respect of Section 8 Companies

*In respect of **Section 8 Companies** which have not committed a default in filing their financial statements under Section 137 or Annual Return under Section 92 with the Registrar, following proviso shall be inserted in Section 186(7):*

'Provided that nothing contained in this sub-section shall apply to a company in which twenty-six per cent or more of the paid-up share capital is held by the Central Government or one or more State Governments or both, in respect of loans provided by such company for funding Industrial Research and Development projects in furtherance of its objects as stated in its memorandum of association'. [Notification No. GSR 466(E), dated 5-6-2015 as amended by Notification No. GSR 584(E), dated 13-6-2017.]

- (vii) **No giving of loan, etc., till default in respect of deposits is subsisting [Section 186 (8)]:** A company which is in default in the repayment of any deposits accepted before or after the commencement of the Companies Act, 2013 or in payment of interest thereon, shall not give any loan or give any guarantee or provide any security or make an acquisition till such default is subsisting.

- (viii) **Maintenance of Register [Section 186 (9)]:** Every company giving loan or giving a guarantee or providing security or making an acquisition shall keep a register. It shall contain such particulars and shall be maintained in such manner as is prescribed in Rule 12 of the Companies (Meetings of Board and its Powers) Rules, 2014. The requirements of Rule 12 are as under:

Every company shall, from the date of its incorporation

- maintain a register in *Form MBP 2* and
- enter the particulars of loans and guarantees given, securities provided and acquisitions made.

The entries in the register shall be made chronologically in respect of each such transaction

- within **7 days** of making loan or giving guarantee or providing security or making acquisition

Maintenance of register

- It shall be kept at the registered office of the company and shall be preserved permanently and shall be kept in the custody of the company secretary of the company or any other person authorised by the Board
- The entries in the register (either manual or electronic) shall be authenticated by the company secretary of the company or by any other person authorised by the Board

furnishing of extracts from register

- The extracts from such register may be furnished to any member on payment of fee prescribed in the Articles which shall not exceed ₹10 for each page.

- (ix) **Non-applicability of Section 186 except sub-section (1) to certain transactions [Section 186 (11)]:** Section 186, (except Section 186 (1)), shall not apply:

- (a) to any loan made, any guarantee given or any security provided or any investment:
- made by a banking company, or an insurance company, or a housing finance company in the ordinary course of its business; or
 - made by a company established with the object of and engaged in the business of financing industrial enterprises, or of providing infrastructural facilities¹⁵;

¹⁵ As per *Explanation (b)* to Section 186 of the Act, the expression “infrastructural facilities” means the facilities specified in Schedule VI.

(b) to any investment—

(i) made by an investment company;

¹⁶**Note:** The expression “investment company” means a company whose principal business is the acquisition of shares, debentures or other securities and a company will be deemed to be principally engaged in the business of acquisition of shares, debentures or other securities, if its assets in the form of investment in shares, debentures or other securities constitute not less than fifty per cent. of its total assets, or if its income derived from investment business constitutes not less than fifty per cent. as a proportion of its gross income

(ii) made in shares allotted in pursuance of Section 62 (1) (a) [i.e. right shares] or in shares allotted in pursuance of rights issues made by a body corporate;

(iii) made, in respect of investment or lending activities, by a non-banking financial company registered under Chapter III-B of the Reserve Bank of India Act, 1934 and whose principal business is acquisition of securities.

(x) **Restriction on the inter-corporate loans/deposits to be taken by companies registered under Section 12 of SEBI [Section 186 (6) and Rule 11 (3)]:** A company registered under Section 12 of the Securities and Exchange Board of India Act, 1992 and covered under such class or classes of companies which may be notified by the Central Government in consultation with the Securities and Exchange Board, shall not take inter-corporate loan or deposits in excess of the limits specified under the regulations applicable to this kind of company, pursuant to which it has obtained certificate of registration from the Securities and Exchange Board of India.

Further, such company shall furnish in its financial statement the details of the loan or deposits.

Note: Section 12 of the SEBI Act, 1992 requires stock broker, sub-broker, share transfer agent, banker to an issue, registrar to an issue, merchant banker, underwriter, portfolio manager, etc. to get registered with SEBI and obtain certificate of registration. There are regulations framed by SEBI which regulate such entities.

(xi) **Punishment for contravention [Section 186 (13)]:** In case of contravention of any of the provisions of Section 186, the punishment shall be as under:

- **Company:** punishable with minimum fine of ₹25,000 and maximum of ₹ 5 lakhs.
- **Every defaulting officer:** punishable with imprisonment maximum up to two years and with fine minimum of ₹25,000 and maximum of ₹1,00,000.

For the purposes of section 186, the expression “infrastructure facilities” means the facilities specified in Schedule VI.

¹⁶ As per Explanation (a) to Section 186 of the Act.

Note: The students may also refer the Companies (Restriction on Number of Layers) Rules, 2017, which have been enforced w.e.f. 20th September 2017.

Exemptions

Section 186 shall not apply to:

- (a) a **Government company** engaged in defence production;
- (b) a **Government company, other than a listed company**, in case such company obtains approval of the Ministry or Department of the Central Government which is administratively in charge of the company, or, as the case may be, the State Government before making any loan or giving any guarantee or providing any security or making any investment under the section.

Note: The above exception is applicable to a Government company which has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar.

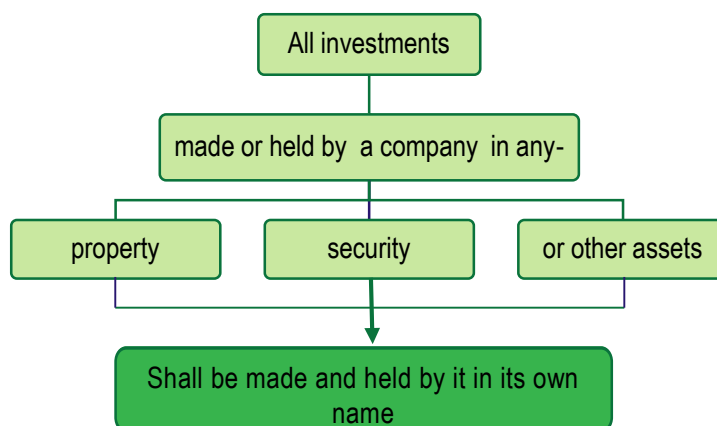
[Notification No. G.S.R. 463 (E), dated 5th June 2015 as amended by Notification No. G.S.R.582 (E), dated 13th June 2017.]



16. INVESTMENTS OF COMPANY TO BE HELD IN ITS OWN NAME [SECTION 187]

Section 187 of the Act contains provisions which, as a general rule, require that all investments made by a company shall be held by it in its own name. There are certain exemptions also. The provisions of Section 187 are discussed as under:

- (i) **Investments by a company in its own name:** According to Section 187 (1), all investments made or held by a company in any property, security or other assets shall be made and held by it in its own name. Following diagram depicts this provision:



As an exception¹⁷, it is provided that company may hold any shares in its subsidiary company in the name of any nominee or nominees of the company, if it is necessary to do so, to ensure that the number of members of the subsidiary company is not reduced below the statutory limit.

(ii) **Exemptions:** It is not always necessary that a company must hold the investments in its own name. Certain exemptions provided by Section 187 (2) are as under:

- (a) **Deposit of shares and debentures with bankers for collection of dividend and interest:** A company is permitted to deposit with its bankers any shares or securities for the collection of any dividend or interest payable thereon.
- (b) **Deposit or transfer to or hold in the name of its bankers shares or securities, in order to facilitate the transfer:** A company is permitted to deposit with or transfer to or hold in the name of its bankers (*i.e.* the State Bank of India or a scheduled bank), shares or securities, in order to facilitate the transfer thereof.

However, if within a period of **6 months** from the date on which the shares or securities are transferred by the company to, or are first held by the company in the name of its bankers (*i.e.* the State Bank of India or a scheduled bank), no transfer of such shares or securities takes place, the company shall, as soon as practicable after the expiry of that period, have the shares or securities re-transferred to it from its bankers or, as the case may be, again hold the shares or securities in its own name.

- (c) **Deposit with or transfer to any person any shares or securities, by way of security for the repayment of any loan :** A company is permitted to deposit with or transfer to any person any shares or securities, by way of security for the repayment of any loan advanced to the company or the performance of any obligation undertaken by it.
- (d) **Depository investments in the form of securities held as a beneficial owner:** A company is permitted to hold investments in the name of a depository when such investments are in the form of securities held by the company as a beneficial owner.

(iii) **Maintenance of Register by a company in case securities are held in the name of a depository and not in its own name [Section 187 (3)]:** Section 187 (2) (d) permits a company to hold securities (*i.e.* any shares or securities) in the name of a depository, the company being the beneficial owner. In this case, though the investment in shares and securities has been made by the company but the securities are not held by it in its own name.

When the above situation arises, the company shall maintain a register which shall contain such particulars as may be prescribed (refer Rule 14 below) and such register shall be open

¹⁷ As per Proviso to Section 187 (1).

to inspection by any member or debenture-holder of the company without any charge during business hours subject to such reasonable restrictions as the company may by its articles or in general meeting impose.

Provisions regarding maintenance of register as per Rule 14: The requirements of Rule 14 of the Companies (Meetings of Board and its Powers) Rules, 2014 are as under:

- (a) **Maintenance of Register:** From the date of its registration, every company shall maintain a register in Form MBP-3.
- (b) **Entry of particulars of investments:** The company shall enter in the register, chronologically, the particulars of investments in shares or other securities beneficially held by the company but which are not held in its own name. It shall also record the reasons for not holding the investments in its own name and the relationship or contract under which the investment is held in the name of any other person.
- (c) The company shall also record whether such investments are held in a third party's name for the time being or otherwise.
- (d) **Place:** The register shall be maintained at the registered office of the company and shall be preserved permanently.
- (e) **Custody of register:** The register shall be kept in the custody of the company secretary of the company or if there is no company secretary, any director or any other officer authorised by the Board.
- (f) **Authentication of entries:** The entries in the register shall be authenticated by the company secretary of the company or by any other person authorised by the Board for the purpose.

Securities held by any person in which the company holds beneficial interest, compliance of section 89 requires declaration in respect of beneficial interest of any securities.

- (iv) **Punishment for contravention [Section 187 (4)]:** If a company is in default in complying with the provisions of this section, the company shall be liable to a penalty of five lakh rupees and every officer of the company who is in default shall be liable to a penalty of fifty thousand rupees.



17. RELATED PARTY TRANSACTIONS [SECTION 188]

Section 188 of the Act along with Rule 15 of the Companies (Meetings of Board and its Powers) Rules, 2014 contain provisions which regulate 'related party transactions'. Further, Section 2(76) of the Act defines who is a 'related party'. These provisions are discussed in the following paragraphs:

(1) Meaning of 'Related Party':

As per Section 2(76), 'related party', with reference to a company, means-

- (i) a director or his relative;

- (ii) a key managerial personnel (KMP) or his relative;
- (iii) a firm, in which a director, manager or his relative is a partner;
- (iv) a private company in which a director or manager or his relative is a member or director;
- (v) a public company in which a director or manager is a director and holds along with his relatives, more than 2% of its paid-up share capital;
- (vi) any body corporate whose Board of Directors, managing director or manager is accustomed to act in accordance with the advice, directions or instructions of a director or manager;
- (vii) any person on whose advice, directions or instructions a director or manager is accustomed to act:

Note: It is provided that sub-clauses (vi) and (vii) shall not apply to the advice, directions or instructions which are given in a professional capacity;

- (viii) any body corporate which is—

- (A) a holding, subsidiary or an associate company of such company;
- (B) a subsidiary of a holding company to which it is also a subsidiary; or
- (C) an investing company or the venturer of the company.

Note: It is clarified by way of *Explanation* that "the investing company or the venturer of a company" means a body corporate whose investment in the company would result in the company becoming an associate company of the body corporate.

Exemption

*In case of a **private company** which has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar sub-clause (viii) of clause 76 of Section 2 shall not apply with respect to Section 188. [Notification No. GSR 464 (E), dated 5th June, 2015 as amended by Notification No. GSR 583 (E), dated 13th June, 2017.]*

- (ix) such other person as may be prescribed (refer Box below).

In this respect, Rule 3 of the Companies (Specification of Definitions Details) Rules, 2014 provides that for the purposes of sub-clause (ix) above, a **director** other than an independent director or **key managerial personnel of the holding company or his relative** with reference to a company, shall be deemed to be a **related party**.

Further, the persons covered under sub-clauses (vi) and (vii) above shall not be related parties if advice, directions or instructions are given by them in a professional capacity.

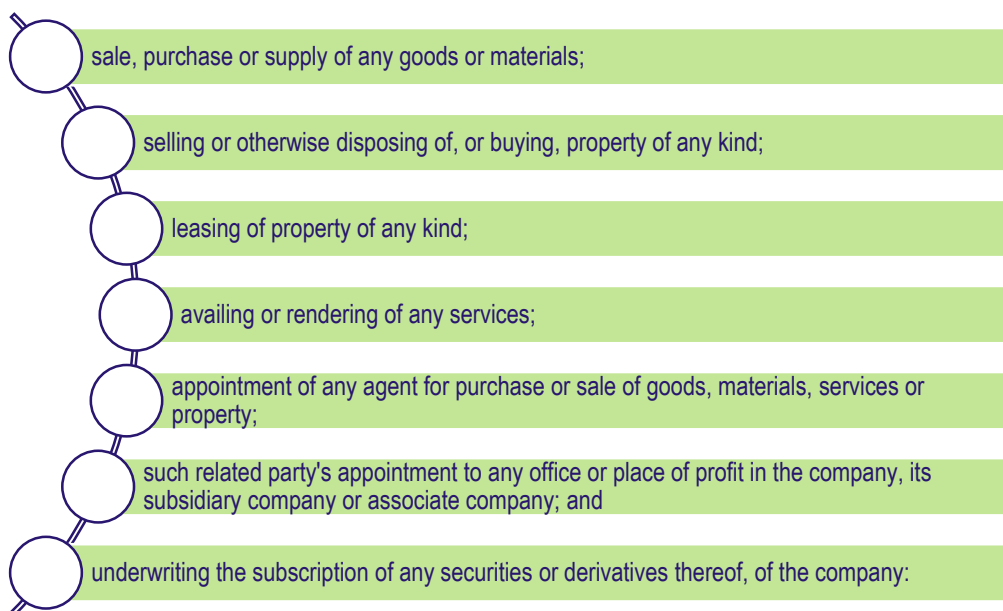
Meaning of 'Relative'

Section 2 (77) of the Act defines the term 'relative'. Accordingly, 'relative', with reference to any person, means any one who is related to another, if—

- (i) they are members of a Hindu Undivided Family;
- (ii) they are husband and wife; or
- ¹⁸(iii) one person is related to the other in the prescribed manner as under:
 - (1) Father (including step-father).
 - (2) Mother (including step-mother).
 - (3) Son (including step-son).
 - (4) Son's wife.
 - (5) Daughter.
 - (6) Daughter's husband.
 - (7) Brother (including the step-brother).
 - (8) Sister (including the step-sister).

- (2) **Related party transactions to which Section 188 is applicable:** Section 188(1) specifies certain transactions (*i.e. contracts or arrangements*) which shall be termed as 'related party transactions' if a company undertakes them with a 'related party'. Such transactions are depicted in the following diagram:

Transactions referred to in sub-section (1) of Section 188:



¹⁸ As per Rule 4 of the Companies (Specification of Definitions Details) Rules, 2014.

¹⁹Meaning of “Office or Place of Profit”

The expression “office or place of profit” means any office or place—

- (1) **where such office or place is held by a director** - if the director holding it receives from the company anything by way of remuneration over and above the remuneration to which he is entitled as director, by way of salary, fee, commission, perquisites, any rent-free accommodation, or otherwise;
- (2) **where such office or place is held by an individual other than a director or by any firm, private company or other body corporate** - if the individual, firm, private company or body corporate holding it receives from the company anything by way of remuneration, salary, fee, commission, perquisites, any rent-free accommodation, or otherwise.

It is noteworthy that **Section 188 does not bar a company from entering into ‘related party transactions’**. They can very well be undertaken, but after following the procedure prescribed as per the law like taking permission from the Board and if required, from the company in general meeting when prescribed limits are exceeded. If the provisions do not require any procedure to be followed, these transactions can also be entered without following the prescribed procedure.

- (3) **Related Party Transactions for which no approval is required [Fourth Proviso to Section 188 (1)]**: In case any related party transaction is entered into by the company in its ordinary course of business and at an arm’s length basis, Section 188 (1) is not attracted and therefore, no approval is required. However, transactions which are not on an arm’s length basis shall require the appropriate approval.

Note: The expression “arm’s length transaction” means²⁰ a transaction between two related parties that is conducted as if they were unrelated, so that there is no conflict of interest.

- (4) **Related Party Transactions requiring consent of the Board²¹**: In case, a related party transaction covered under Section 188 (1) (i.e. contract or arrangement between a company and related party) is not on arm’s length basis and also does not require approval of the shareholders, it shall be entered into by the company after obtaining consent of the Board of Directors given by a resolution at a meeting of the Board and subject to the conditions as prescribed by Rule 15 (1) of the Companies (Meetings of Board and its Powers) Rules, 2014.

¹⁹ As per *Explanation (a)* to Section 188 (1) of the Act.

²⁰ As per *Explanation (b)* to Section 188 (1) of the Act.

²¹ As per Section 188 (1) of the Act.

According to Rule 15 (1), if a company enters into a transaction with a related party, the agenda of the Board meeting at which the resolution is proposed to be moved shall disclose the **following matters**:

- (a) the name of the related party and nature of relationship;
- (b) the nature, duration of the contract and particulars of the contract or arrangement;
- (c) the material terms of the contract or arrangement including the value, if any;
- (d) any advance paid or received for the contract or arrangement, if any;
- (e) the manner of determining the pricing and other commercial terms, both included as part of contract and not considered as part of the contract;
- (f) whether all factors relevant to the contract have been considered, if not, the details of factors not considered with the rationale for not considering those factors; and
- (g) any other information relevant or important for the Board to take a decision on the proposed transaction.

Note: According to Rule 15 (2), in case any director is interested in any contract or arrangement with a related party, he shall not be present at the meeting during discussions on the resolution relating to such contract or arrangement-

- (5) (i) **Related Party Transactions requiring approval by ordinary resolution²²:** In case a company enters into a contract or arrangement with a related party and the value of transaction exceeds the prescribed value as per Rule 15 (3), it shall be entered into with the prior approval of the company by passing an ordinary resolution.

The provisions of Rule 15(3) are explained as under:

- (A) Approval by an ordinary resolution is required where the transaction or transactions to be entered into as contracts or arrangements with respect to clauses (a) to (e) of Section 188 (1) are as per the following criteria:

Details of transactions to be entered into as contracts or arrangements with respect to clauses (a) to (e) of sub-section (1) of Section 188	Prescribed limits for seeking approval by a resolution relating to the specified transactions
(i) Sale, purchase or supply of any goods or materials, directly or through appointment of agent,	If the value of such transaction or transactions amounting to 10% or

²² As per First Proviso to Section 188 (1) and Rule 15 (3) of the Companies (Meetings of Board and its Powers) Rules, 2014.

as mentioned in clause (a) and clause (e) respectively of sub-section (1) of Section 188.	more of the turnover of the company. Note: Above limit shall apply for transaction or transactions to be entered into either individually or taken together with the previous transactions during a financial year.
(ii) Selling or otherwise disposing of or buying property of any kind, directly or through appointment of agent, as mentioned in clause (b) and clause (e) respectively of sub-section (1) of Section 188.	If the value of such transaction or transactions amounting to 10% or more of net worth of the company. Note: Above limit shall apply for transaction or transactions to be entered into either individually or taken together with the previous transactions during a financial year.
(iii) Leasing of property of any kind , as mentioned in clause (c) of sub-section (1) of Section 188.	If the value of such transaction or transactions amounting to ten per cent or more of the turnover of the company. Note: Above limit shall apply for transaction or transactions to be entered into either individually or taken together with the previous transactions during a financial year.
(iv) Availing or rendering of any services , directly or through appointment of agent, as mentioned in clause (d) and clause (e) respectively of sub-section (1) of section 188.	If the value of such transaction or transactions amounting to 10% or more of the turnover of the company. Note: Above limit shall apply for transaction or transactions to be entered into either individually or taken together with the previous transactions during a financial year.

- (B) Where the transaction or transactions to be entered into as contract or arrangement is for **appointment to any office or place of profit in the company**, its subsidiary company or associate company at a monthly remuneration **exceeding ₹2.5 lakh rupees as mentioned in clause (f) of sub-section (1) of Section 188**, approval by an ordinary resolution is required.

- (C) Where the transaction or transactions to be entered into as contract or arrangement is **for remuneration for underwriting** the subscription of any securities or derivatives thereof, of the company **exceeding 1% of the net worth as mentioned in clause (g) of sub-section (1) of Section 188**, approval by an ordinary resolution is required.

²³**Note 1: Turnover or Net Worth:** The turnover or net worth shall be computed on the basis of the audited financial statement of the preceding financial year.

²⁴**Note 2: The explanatory statement to be annexed to the notice** of a general meeting convened pursuant to Section 101 shall contain the following particulars, namely:

- (a) name of the related party;
- (b) name of the director or key managerial personnel who is related, if any;
- (c) nature of relationship;
- (d) nature, material terms, monetary value and particulars of the contract or arrangement;
- (e) any other information relevant or important for the members to take a decision on the proposed resolution."

- (ii) **No voting by a related member [Second Proviso to Section 188(1)]:** A member of the company who is a related party shall not vote on the resolution meant for approving any contract or arrangement which may be entered into by the company.

²⁵**Note:** However, nothing contained in the second proviso shall apply to a company in which ninety per cent or more members, in number, are relatives of promoters or are related parties.

Exemptions

1. *First and Second Proviso to Section 188(1) shall not apply to:*
 - (a) a **government company** in respect of contracts or arrangements entered into by it with any other government company;
 - (b) a **government company**, other than a listed company, in respect of contracts or arrangements other than those referred to in clause(a), in case such company obtains approval of the Ministry or Department of the Central Government which is

²³ As per Explanation (1) to Rule 15 (3).

²⁴ As per Explanation (3) to Rule 15 (3).

²⁵ As per Third Proviso to Section 188 (1).

administratively in charge of the company, or as the case may be, the state Government before entering into such contract or arrangement.

Note: The above exemption is applicable to a Government company which has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar.

[Notification No. G.S.R. 463(E), dated 5th June 2015 as amended by Notification No. G.S.R. 582(E), dated 13th June 2017.]

2. Second Proviso to Section 188(1) **shall not apply to a private company** provided it has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar.

Note: This exemption implies that a member of a private company is permitted to vote on the resolution irrespective of the fact that such member is a related party.

[Notification No. G.S.R. 464(E), dated 5th June 2015 as amended by Notification No. G.S.R. 583(E), dated 13th June 2017.]

Scope of Second Proviso to Section 188(1) - Clarification

The second proviso to sub-section (1) of Section 188 requires that **no member of the company shall vote on a resolution** to approve the contract or arrangement (referred to in the first proviso), if such a member is a related party.

The MCA has clarified that 'related party' referred to in the Second Proviso has to be construed with reference only to the contract or arrangement for which the said resolution is being passed.

Thus, the term '**related party**' in the above context refers only to such related party as may be a related party in the context of the contract or arrangement for which the said resolution is being passed. [General Circular No. 30/2014, dated 17th July, 2014]

- (6) **Transactions between a holding company and its wholly owned subsidiary [Fifth Proviso to Section 188 (1)]:** In case transactions are entered into between a holding company and its wholly owned subsidiary whose accounts are consolidated with such holding company and placed before the shareholders at the general meeting, there is no need for seeking approval of the company by passing an ordinary resolution by the members.

Explanation (2) to Rule 15 (3) states that in case of a wholly owned subsidiary, the resolution passed by the holding company shall be sufficient for the purpose of entering into the transactions between the wholly owned subsidiary and the holding company.

- (7) **Related party transactions voidable at the option of the Board/shareholders [Section 188 (3)]:** A contract or arrangement shall be voidable at the option of the Board or, as the case may be, of the shareholders:

- (a) **Contract/arrangement entered without obtaining the consent of the Board or approval by a resolution:** Where any contract or arrangement is entered into by a director or any other employee, without obtaining the consent of the Board or approval by a resolution in the general meeting as required under Section 188 (1), and

No ratification by Board/shareholders: if it is not ratified by the Board or, as the case may be, by the shareholders at a meeting within 3 months from the date on which such contract or arrangement was entered into.

Further, if the contract or arrangement is with a related party to any director, or is authorised by any other director, the directors concerned shall indemnify the company against any loss incurred by it.

- (b) **Company may proceed to recover loss in contravention of the provisions of this section:** Section 188 (4) provides that it shall be open to the company to proceed against a director or any other employee who had entered into such contract or arrangement in contravention of the provisions of Section 188 for recovery of any loss sustained by it as a result of such contract or arrangement.

- (8) **Punishment for contravention [Section 188 (5)]:** Any director or any other employee of a company who had entered into the contract or arrangement, or authorised it, in violation of the provisions of Section 188 shall be punishable as under:

In the case of	Punishment
Listed company	liable to a penalty of twenty-five lakh rupees, and
Any other company	liable to a penalty of five lakh rupees

- (9) **Disclosures of 'related party transactions' in Board's report [Section 188 (2)]:** Every contract or arrangement entered into under Section 188 (1) (i.e. the related party transactions) shall be mentioned in the Board's report to the shareholders along with the justification for entering into such contract or arrangement.

Applicability of Section 188 to Corporate Restructuring, Amalgamations etc.

The MCA has clarified that transactions arising out of Compromises, Arrangements and Amalgamations dealt with under specific provisions of the Companies Act, 2013, will not attract the requirements of Section 188 of the Companies Act, 2013. [General Circular No. 30/2014, dated 17th July, 2014]

1. The National Company Law Tribunal, of Kochi Bench in *Sulochana Gupta v. RBG Enterprises (P.) Ltd.* Passed an order under Section 188 of the Companies Act. It was held that where directors of company have siphoned huge amounts from company in pretext of remuneration to themselves and to their spouses (full time employees assisting company) without approval of majority of shareholders, was related party transactions and said to be contrary to provisions of law and in breach of Articles of Association of company and thus, were held to be declared as invalid.

2. The High Court of Madras in *Vikramjit Singh Oberoi v. Registrar of Companies* held that payment of royalty is a license fees for use of brand/trade name, same do not qualify as contract related to sale, purchase or supply of goods, materials or services and therefore, section 188 does not apply.

Further with respect to Financial Statement, Board's report, etc. where company had availed services, such as car rentals, laundry services etc. from related party in ordinary course of business on an arm's length basis, it was held that company was not required to disclose same in its board report as per the requirement of section 134 read with 188 of the Companies Act, 2013.

18. REGISTER OF CONTRACTS OR ARRANGEMENTS IN WHICH DIRECTORS ARE INTERESTED [SECTION 189]

Section 189 of the Act, contains provisions for maintenance of Register of contracts or arrangements in which directors are interested. According to this section:

- (i) **Maintenance of register of contracts or arrangements [Section 189(1)]:** It is mandatory for all companies to keep one or more registers giving separately the particulars of all contracts or arrangements as required under:
 - (a) Section 184(2) [Disclosure of Interest by Directors]; or
 - (b) Section 188 [Related Party Transactions].
- (ii) **Manner of preparation of register:** Such register shall be prepared in the prescribed manner and shall contain prescribed particulars. [Section 189(1)]

As regards prescribed manner and particulars, we may refer Rule 16 of the Companies (Meetings of Board and its Powers) Rules, 2014 which states that the Register of contracts or arrangements shall be maintained in Form No. MBP 4. The company concerned shall enter therein:

- the particulars of company or companies or bodies corporate, firms or other association of individuals, in which any director has any concern or interest, as mentioned under Section 184 (1).

As an exception, the particulars of the company or companies or bodies corporate in which a director himself together with any other director **holds two percent or less of the paid-up share capital** would not be required to be entered in the register.

- the particulars of contracts or arrangements with a body corporate or firm or other entity as mentioned under Section 184 (2), in which any director is, directly or indirectly, concerned or interested; and
 - the particulars of contracts or arrangements with a related party with respect to transactions to which Section 188 applies.
- (iii) **When to make entries in the Register:** As per Rule 16, the entries in the Register shall be made at once and in the chronological order. They shall be authenticated by the Company secretary or any other person authorised by the Board.
- (iv) **Register to be signed [Section 189(1)]:** The register, after being duly filled and updated, shall be placed before the next meeting of the Board and signed by all the directors present at the meeting.
- (v) **Disclosure to be made by a director or KMP [Section 189(2)]:** Every director or key managerial personnel (KMP) shall, within a period of 30 days of his appointment, or relinquishment of his office, as the case may be, disclose the particulars specified in Section 184(1) relating to his concern or interest in the other associations which are required to be included in the register or such other information relating to himself as may be prescribed.
- (vi) **Register to be kept at registered office [Section 189(3)]:** The register shall be kept at the registered office of the company and it shall remain open for inspection at such office during business hours.
- (vii) **Preservation and custody:** According to Rule 16 (3), the register shall be preserved permanently and shall be kept in the custody of the Company Secretary or any other person authorised by the Board for the purpose.
- (viii) **Extracts from register [Section 189(3) and Rule 16 (4)]:** The company shall provide extracts from such register to a member of the company on his request, within seven days from the date on which such request is made upon the payment of such fee as may be specified in the articles of the company, subject to a maximum of ₹10 per page.
- (ix) **Register to be produced at AGM [Section 189(4)]:** The register shall be produced at the commencement of every annual general meeting (AGM). It shall remain open and accessible during the continuance of the meeting to any person having the right to attend the meeting. Thus, even a proxy has a right to inspect the Register.
- (x) **Exceptions [Section 189(5)]:** Section 189(1) shall not apply to any contract or arrangement i.e. the particulars of a contract or arrangement shall not be entered in the Register-
- (a) if it is for the **sale, purchase or supply of any goods, materials or services** and the value of such goods and materials or the cost of such services **does not exceed ₹ 5,00,000 in the aggregate in any year**; or

- (b) if it is entered into by a **banking company for the collection of bills** in the ordinary course of its business.
- (xi) **Penalty for contravention [Section 189(6)]**: Every director who fails to comply with the provisions of Section 189 regarding maintenance of 'Register of contracts or arrangements in which directors are interested' and the Rules made there under shall be liable to a penalty of ₹ 25,000.

*In respect of a **Section 8 company** which has not committed a default in filing its financial statements under Section 137 or Annual Return under Section 92 with the Registrar, the provisions of Section 189 shall apply only if the transaction with reference to Section 188 on the basis of terms and conditions of the contract or arrangement **exceeds one lakh rupees**. [Notification No. G.S.R. 466(E), dated 5th June 2015 as amended by Notification No. G.S.R. 584 (E), dated 13th June, 2015.]*



19. CONTRACT OF EMPLOYMENT WITH MANAGING OR WHOLE- TIME DIRECTORS [SECTION 190]

A Company may enter into a contract of employment with managing or whole-time directors. Section 190 of the Act contains provisions relating to keeping of such contract of employment. These provisions are stated as under:

- (i) **Maintenance of copy of contract of employment**: Every company shall keep at its registered office,—
- (a) **where a contract of service with a managing or whole-time director is in writing**, a copy of the contract; or
 - (b) **where such a contract is not in writing**, a written memorandum setting out its terms.
- (ii) **Inspection**: The copies of the contract or the memorandum shall be open to inspection by any member of the company without payment of fee.
- (iii) **Penalty for non-compliance [Section 190 (3)]**: If any default is made in complying with Section 190, the penalty shall be as under:
- **Company**: liable to a penalty of ₹ 25,000 for each default
 - **Every defaulting officer**: liable to a penalty of ₹ 5,000 for each default.
- (iv) **Exception [Section 190 (4)]**: The provisions of Section 190 shall not apply to a **private company**.



20. PAYMENT TO DIRECTOR FOR LOSS OF OFFICE, ETC., IN CONNECTION WITH TRANSFER OF UNDERTAKING, PROPERTY OR SHARES [SECTION 191]

Section 191 of Act, applicable to all companies, contains provisions which regulate payment to the directors for loss of office, etc., in connection with transfer of undertaking, property or shares by a company. These provisions are discussed as under:

- (i) **No compensation except after specific disclosures and after approval of payment proposal by members:** Section 191(1) enumerates happening of certain specific events in relation to a company and also states, *inter-alia*, whether or not any director of that company shall receive compensation, etc. on happening of such events. These events are given as under:
- (a) the **transfer** of the whole or any part of any **undertaking or property** of the company; or
 - (b) the **transfer** to any person of all or any of the **shares** in a company being a transfer resulting from—
 - (i) an offer made to the general body of shareholders.
 - (ii) an offer made by or on behalf of some other body corporate with a view to a company becoming a subsidiary company of such body corporate or a subsidiary company of its holding company;
 - (iii) an offer made by or on behalf of an individual with a view to his obtaining the right to exercise, or control the exercise of, not less than 1/3rd of the total voting power at any general meeting of the company; or
 - (iv) any other offer which is conditional on acceptance to a given extent,

Disclosure of particulars and approval in general meeting: In connection with above events, a **director of a company** shall not receive any payment **unless** particulars as may be prescribed (*refer Rule 17 below*) with respect to the payment proposed to be made by the transferee or person, including the amount thereof, have been disclosed to the members of the company and the proposal has been approved by the company in general meeting.

Subject to the conditions of disclosure and approval as mentioned above, a director of a company may receive payment:

- by way of compensation for loss of office, or
- as consideration for retirement from office, or
- in connection with such loss or retirement from such company, or

- from the transferee of such undertaking or property, or
- from the transferees of shares or
- from any other person, not being such company.

According to **Rule 17 (1)** of the Companies (Meetings of Board and its Powers) Rules, 2014, the specified particulars which need to be disclosed to the members of the company for approving the proposal by passing a resolution at a general meeting are as under:

- (a) name of the director;
 - (b) amount proposed to be paid;
 - (c) event due to which compensation becomes payable;
 - (d) date of Board meeting recommending such payment;
 - (e) basis for the amount determined;
 - (f) reason or justification for the payment;
 - (g) manner of payment - whether payable in cash or otherwise and how;
 - (h) sources of payment; and
 - (i) any other relevant particulars as the Board may think fit.
- (ii) **Payment lawful if within prescribed limits [Section 191 (2)]:** Any payment made by a company to a MD or WTD or manager of the company by way of compensation for loss of office or as consideration for retirement from office or in connection with such loss or retirement shall be considered as lawful if it is subject to limits or priorities as prescribed in Rule 17 (2) of the Companies (Meetings of Board and its Powers) Rules, 2014.
- According to Rule 17 (2), such payment, to be lawful, shall not exceed the limit as set out under Section 202.
- (iii) **No compensation payable under specific circumstances:** According to Rule 17 (3), no compensation shall be paid to the MD or WTD or manager of the company for the loss of office or as consideration for retirement from office (except 'notice pay' and 'statutory payments' according to the terms of their appointment) or in connection with such loss or retirement if:
- (a) the **company is in default** in repayment of **public deposits or payment of interest thereon**;
 - (b) the company is in default in **redemption of debentures** or payment of interest thereon;
 - (c) the company is in default in **repayment of any liability**, secured or unsecured, payable to any bank, public financial institution or any other financial institution;

- (d) the company is in default in **payment of any dues towards** income tax, VAT, excise duty, service tax or any other tax or duty, by whatever name called, payable to the Central Government or any State Government, statutory authority or local authority (other than in cases where the company has disputed the liability to pay such dues);
 - (e) there are **outstanding statutory dues to the employees or workmen** of the company which have not been paid by the company (other than in cases where the company has disputed the liability to pay such dues); and
 - (f) the company has **not paid dividend** on preference shares or not redeemed preference shares on due date.
- (iv) **Payment proposal cannot be taken as approved if no quorum present [Section 191 (3)]:** If the payment is not approved for want of quorum either in a meeting or an adjourned meeting, the proposal shall not be deemed to have been approved.
- (v) **Receipt of payment in contravention of Section 191 (1) [Section 191 (3)]:** In case a director of a company receives payment of any amount in contravention of Section 191 (1) or the proposed payment is made before it is approved in the meeting, the amount so received by the director shall be deemed to have been received by him in trust for the company.
- In other words, the director shall not own such amount but keep it as trustee of the company.
- (vi) **Penalty for non-compliance [Section 191 (5)]:** If a director of the company makes any default in complying with the provisions of Section 191, he shall be liable to a penalty of **one lakh rupees**.
- (vii) **No effect on disclosures [Section 191 (6)]:** Section 191 shall not be taken to prejudice the operation of any law requiring disclosure to be made with respect to any payment received under Section 191 or such other like payments made to a director. In other words, if required by any law, the disclosures regarding any payment of compensation shall be made.

Note: Due to the notifying of Section 247 (1) w.e.f. 18-10-2017, the valuation of stocks, shares, debentures, securities, etc. will be conducted by a Registered Valuer as appointed by the Audit Committee or in its absence by the Board of Directors. Before this, it was being conducted by an independent merchant banker registered with SEBI or an independent chartered accountant in practice having a minimum experience of ten years.

21. RESTRICTION ON NON-CASH TRANSACTIONS INVOLVING DIRECTORS [SECTION 192]

Section 192 of the Act places restrictions on the non-cash transactions involving directors and the company or *vice-versa*. The provisions of Section 192 also operate if non-cash transactions involve

a person who is a director of the company's holding, subsidiary or ²⁶associate company. A person connected with any such director is also included. These provisions are discussed as under:

- (i) **Restriction on acquiring assets for consideration other than cash:** According to Section 192 (1), no company shall enter into an arrangement by which—
 - (a) **a director of the company or its holding, subsidiary or associate company or a person connected with him acquires** or is to acquire assets for consideration other than cash, from the company; or
 - (b) **the company acquires** or is to acquire assets for consideration other than cash, from such director or person so connected.
- (ii) **Relaxation of restriction:** The above restriction shall be relaxed *i.e.* the company may enter into an arrangement involving non-cash transactions as stated in clause (i) above, if prior approval for such arrangement is accorded by a resolution of the company in general meeting.

Where the director or connected person is a director of its holding company, approval shall also be required to be obtained by passing a resolution in general meeting of the holding company.
- (iii) **Contents of notice issued for approval of resolution:** The notice for approval of the resolution in general meeting issued by the company or holding company shall include the particulars of the arrangement. It shall also include the value of the assets involved in such arrangement duly calculated by a registered valuer.
- (iv) **What happens if Section 192 is contravened:** Any arrangement entered into by a company or its holding company in contravention of the provisions of Section 192 shall be voidable at the instance of the company. The arrangement shall not be voidable;
 - (a) if the restitution of any money or other consideration which is the subject-matter of the arrangement is no longer possible and the company has been indemnified by any other person for any loss or damage caused to it; or
 - (b) if any rights are acquired *bona fide* for value and without notice of the contravention of the provisions of this section (*i.e.* Section 192) by any other person.

²⁶ An associate company is defined by Section 2 (6) of the Act. Accordingly, an 'associate company' in relation to another company, means a company in which that other company has a significant influence, but which is not a subsidiary company of the company having such influence and includes a joint venture company.

Explanation: For the purpose of this clause,

- (a) the expression 'significant influence' means control of at least 20% of total voting power, or control of or participation in business decisions under an agreement;
- (b) the expression 'joint venture' means a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement.



22. CONTRACTS BY ONE PERSON COMPANY (OPC) [SECTION 193]

Section 193 of Act contains provisions in respect of contracts entered into by a One Person Company (OPC) which is limited by shares or by guarantee. This section becomes applicable when such OPC enters into a contract with its sole member who is also its director. Section 193 operates in the following manner:

- (i) Preferably, such contract should be in **writing**.
- (ii) If not in writing, the OPC shall ensure that the **terms of the contract or offer are contained in a memorandum or are recorded in the minutes** of the first meeting of the Board of Directors of the company held next after entering into contract.
- (iii) **Exception:** If the contracts are entered into by the company in the ordinary course of its business then provisions of Section 193 are not applicable.
- (iv) **Submission of information to the registrar:** The company shall inform the Registrar about every such contract entered into by the company and recorded in the minutes of the meeting of its Board of Directors. This shall be done within a period of 15 days of the date of approval by the Board.

TEST YOUR KNOWLEDGE**Multiple Choice Questions**

1. Chetan Motorboats Limited, incorporated on 25th June, 2019 is desirous of making donations to a reputed political party. Out of the following options, choose the one which correctly depicts as to when Chetan Motorboats Limited shall be eligible to make such donations to a political party:
 - (a) Chetan Motorboats Limited shall be eligible to make donations to a political party after one year from the date of its incorporation.
 - (b) Chetan Motorboats Limited shall be eligible to make donations to a political party after two years from the date of its incorporation.
 - (c) Chetan Motorboats Limited shall be eligible to make donations to a political party after three years from the date of its incorporation.
 - (d) Chetan Motorboats Limited shall be eligible to make donations to a political party after five years from the date of its incorporation.
2. Out of the total strength of six Directors of SQ Transformers Limited, five are attending a Board Meeting to consider the investment of funds of the company. The resolution relating to investment shall be taken as passed in which of the following cases:
 - (a) When all the five Directors of SQ Transformers Limited attending the meeting consent to such investment of funds.
 - (b) When any four Directors of SQ Transformers Limited out of five attending the meeting consent to such investment of funds.
 - (c) When any three Directors of SQ Transformers Limited out of five attending the meeting consent to such investment of funds.
 - (d) Investment proposal must be consented to by the total strength of six Directors of SQ Transformers Limited.
3. The Board of Directors of Shanta Hospitality Services Limited is desirous of contributing certain amount to Ashirwad Dharmarth Sansthan, a bona fide charitable organization operating in the National Capital Region, during the financial year 2021-2022. The profits and losses of the earlier five financial years are as under:

Year	Profit/ (Loss)
2020-2021	(30,00,000)
2019-2020	1,80,00,000
2018-2019	2,10,00,000
2017-2018	1,85,00,000
2016-2017	1,40,00,000

From the following four options, select the appropriate one which indicates the amount that the Board of Directors of Shanta Hospitality Services Limited can contribute to Ashirwad Dharmarth Sansthan:

- (a) The Board of Directors of Shanta Hospitality Services Limited cannot contribute any amount to Ashirwad Dharmarth Sansthan in the financial year 2021-2022 since it suffered losses of Rs. 30,00,000 in the immediate previous financial year 2020-2021.
 - (b) The Board of Directors of Shanta Hospitality Services Limited can contribute maximum of Rs. 9,00,000 to Ashirwad Dharmarth Sansthan in the financial year 2021-2022.
 - (c) The Board of Directors of Shanta Hospitality Services Limited can contribute maximum of Rs. 6,00,000 to Ashirwad Dharmarth Sansthan in the financial year 2021-2022.
 - (d) The Board of Directors of Shanta Hospitality Services Limited can contribute maximum of Rs. 3,00,000 to Ashirwad Dharmarth Sansthan in the financial year 2021-2022.
4. A seven days' notice of the Board Meeting was served on all the ten directors of Goodluck Publishers Limited by sending it on their registered postal addresses. However, before the holding of scheduled Board Meeting, some unavoidable happenings took place. Mr. M was hospitalised because of serious stomach pain just two days before the Meeting. Mr. Y proceeded to London since his son met with an accident and the incidence required his immediate presence. As scheduled earlier, Mr. X and Mr. B went to Australia for attending a technical seminar that would help improving the existing publishing techniques. Mr. A, extremely busy in finalizing the arrangements relating to his daughter's marriage, was also unable to attend the impending board meeting. A day before the board meeting, Mr. E's grand-mother got hospitalised and therefore, he was involved in taking care of her but he assured to attend the meeting through video conferencing. Mr. P was scheduled to arrive for the meeting by 2 p.m. on the same day of the meeting but his flight got delayed by eight hours. Mr. D, Mrs. G and Mr. H were in the town and were available for the Board Meeting. Could the Board Meeting be held as per the scheduled time?

- (a) The Board Meeting cannot be held because minimum sixty percent directors (i.e. 6 out of 10) must attend it at the scheduled time to complete the quorum.
 - (b) The Board Meeting cannot be held because minimum fifty percent directors (i.e. 5 out of 10) must attend it at the scheduled time to complete the quorum.
 - (c) Since the quorum is complete, the available directors can hold the Board Meeting as per the schedule.
 - (d) The Board Meeting cannot be held because minimum seventy percent directors (i.e. 7 out of 10) must attend it at the scheduled time to complete the quorum.
5. Seafood Marketing Limited, incorporated on 1st April, 2019, conducted four Board Meetings during the Financial Year 2019-20 i.e. on 6th April, 2019, 28th August, 2019, 30th September, 2019 and 30th March, 2020. Select the correct option from those given below as to whether there is contravention of provisions or not regarding frequency of holding the Board Meetings by Seafood Marketing Limited:
- (a) There is no contravention of the provisions relating to holding of Board Meetings because four Board Meetings have been held by Seafood Marketing Limited during the Financial Year 2019-20.
 - (b) There is no contravention of the provisions relating to holding of Board Meetings by Seafood Marketing Limited because the first Board Meeting was held within 30 days of the incorporation of the company.
 - (c) There is contravention of provisions in respect of conduct of the Board Meetings by Seafood Marketing Limited because gap between initial two consecutive Board Meetings (held on 6th April, 2019 and 28th August, 2019) is 143 days and further, gap between next two consecutive Board Meetings (held on 30th September, 2019 and 12th March, 2020) is 163 days.
 - (d) There is contravention of provisions in respect of conduct of the Board Meetings by Seafood Marketing Limited because gap between initial two consecutive Board Meetings (held on 6th April, 2019 and 28th August, 2019) is 123 days and further, gap between next two consecutive Board Meetings (held on 30th September, 2019 and 12th March, 2020) is 143 days.

Descriptive Questions

1.
 - (i) What is the procedure to be followed, when a board meeting is adjourned for want of quorum?
 - (ii) How is a resolution by circulation passed by the Board or its Committee?
2. Mr. P and Mr. Q who are the directors of C-Tech Limited informed the company about their inability to attend the Board meeting because the notice thereof was not served on them.

Discuss whether there is any default on the part of C-Tech Limited and the consequences thereof.

3. *A director goes abroad for a period of more than 3 months and an alternate director has been appointed in his place under Section 161(2). During the period of absence of the original director, a board meeting was called. In this connection, with reference to the provisions of the Companies Act, 2013, advise who should be given the notice of Board meeting i.e. the "original director" or the "alternate director"?*
4. *Examine with reference to the provisions of the Companies Act, 2013 whether notice of a Board Meeting is required to be sent to the following persons:*
 - (i) *An interested Director;*
 - (ii) *A Director who has expressed his inability to attend a particular Board Meeting;*
 - (iii) *A Director who has gone abroad (for less than 3 months).*
5. *Out of the powers exercisable by the Board under Section 179 of the Companies Act, 2013, the Board of MN Limited wants to delegate the power to borrow monies otherwise than on debentures to the Managing Director. Advise whether such a delegation is possible? Would your answer be different, if the delegation is made to the manager or any other principal officer including a branch officer of the company?*
6. *Advise the Board of Director of Spectra Papers Ltd. regarding validity and extent of its powers, under the provisions of the Companies Act, 2013 in relation to the following matters:*
 - (i) *Buy-back, for the first time, the shares of the Company upto 10% of the paid-up equity share capital without passing a special resolution.*
 - (ii) *Delegation of power to the Managing Director so that he can invest surplus funds of the company in the shares of some other companies.*
7. *An Audit Committee of a listed company constituted under Section 177 of the Companies Act, 2013, submitted its report containing the recommendations in respect of certain matters to the Board. The Board, however, did not accept the recommendations. In the light of the situation, analyze whether:*
 - (a) *The Board is empowered not to accept the recommendations of the Audit Committee.*
 - (b) *If so, what alternative course of action, would the Board resort to?*
8. *MNC Ltd., a company, whose paid up capital was ` 8.00 crore, has issued right shares in the ratio of 1:1. The said company is listed with Mumbai Stock Exchange. Whether the company is required to appoint any Audit Committee and if yes, draft a suitable Board Resolution to appoint an Audit committee covering the aspects as provided in the Companies Act, 2013.*
9. *The Balance Sheets of last three years of PTL Ltd., contain the following information and figures:*

	As at 31.03.2017	As at 31.03.2018	As at 31.03.2019
	₹	₹	₹
Paid up capital	50,00,000	50,00,000	75,00,000
General Reserve	40,00,000	42,50,000	50,00,000
Credit Balance in Profit & Loss Account	5,00,000	7,50,000	10,00,000
Debenture Redemption Reserve	15,00,000	20,00,000	25,00,000
Securities Premium	2,00,000	2,00,000	2,00,000
Secured Loans	10,00,000	15,00,000	30,00,000

On going through other records of the Company, the following is also determined:

Net Profit for the year (as calculated in accordance with the provisions of the Companies Act, 2013)	12,50,000	19,00,000	34,50,000

In the ensuing Board Meeting scheduled to be held on 5th September, 2019, among other items of agenda, following items are also appearing:

- (i) To decide about borrowing from financial institutions on long-term basis.
- (ii) To decide about contributions to be made to charitable funds.

Based on above information, you are required to find out as per the provisions of the Companies Act, 2013, the amount upto which the Board can borrow from Financial institution and the amount upto which the Board of Directors can contribute to Charitable funds during the financial year 2019-20 without seeking the approval in general meeting.

10. Following data relates to Prince Company Limited:

Authorised Capital (Equity Shares)	₹ 100 crore
Paid – up Share Capital	₹ 40 crore
General Reserves	₹ 20 crore
Debenture Redemption Reserve	₹ 10 crore
Provision for Taxation	₹ 5 crore
Securities premium	₹ 2 crore
Loan (Long Term)	₹ 10 crore
Short Term Creditors	₹ 3 crore

Board of Directors of the company by a resolution passed at its meeting decided to borrow an additional sum of ₹ 90 crore from the company's Bankers. Being the company's financial advisor, you are required to advise the Board of Directors regarding the procedure to be followed in this respect under the Companies Act, 2013.

11. One of the Objects Clauses of the Memorandum of Association of Info Limited conferred upon the company power to sell its undertaking to another company with identical objects. Company's Articles also conferred upon the directors whereby power was conferred upon them to sell or otherwise deal with the property of the company. At an Extraordinary General Meeting of the company, members passed an ordinary resolution for the sale of its assets on certain terms and authorized the directors to carry out the sale. Directors refused to comply with the wishes of the members whereupon it was contended on behalf of the members that they were the principals and directors being their agents, were bound to give effect to their (members') decisions.

Examining the provisions of the Companies Act, 2013, answer the following:

Whether the contention of members against the non-compliance of members' decision by the directors is tenable?

Whether it is possible for the members to usurp the powers which by the Articles are vested in the directors by passing a resolution in the general meeting?

12. (i) R Ltd. wants to constitute an Audit Committee. Draft a board resolution covering the following matters [compliance with Companies Act, 2013 to be ensured].
- (1) Members of the Audit Committee
 - (2) Chairman of the Audit Committee
 - (3) Any 2 functions of the said Committee
- (ii) What would be the minimum likely turnover or capital of this company?
- (iii) What is the role of the Audit Committee vis-a-vis the statutory auditor when the company wishes to engage them to perform certain engagements which are not restricted under Section 144?

ANSWERS

Answer to Multiple Choice Questions

1.	c	2.	a	3.	c	4.	c	5.	c

Answer to Descriptive Questions

1. (i) Section 174(4) of the Companies Act, 2013 provides that, if a Board meeting could not

be held for want of quorum, then, unless the articles otherwise provide, the meeting shall automatically stand adjourned to the same day in the next week, at the same time and place, or if that day is a national holiday, till the next succeeding day which is not a national holiday, at the same time and place.

- (ii) (a) The Companies Act, 2013 permits a decision of the Board of Directors to be taken by means of a resolution by circulation. Board's approvals can be taken in two ways - one, by a resolution passed at a Board Meeting and the other, by means of a resolution passed by circulation.

In terms of Section 175(1) of the Companies Act, 2013 no resolution shall be deemed to have been duly passed by the Board or by a committee thereof by circulation, unless the following provisions have been complied with:

- (1) the resolution has been circulated in draft, together with the necessary papers, if any,
- (2) the draft resolution has been circulated to all the directors, or members of the committee, as the case may be;
- (3) the Draft resolution has been sent at their addresses registered with the company in India;
- (4) such delivery has been made by hand or by post or by courier, or through prescribed electronic means;

Rule 5 of the *Companies (Meetings of Board and its Powers) Rules, 2014* provides that a resolution in draft form may be circulated to the directors together with the necessary papers for seeking their approval, by electronic means which may include E-mail or fax.

- (5) such resolution has been approved by a majority of the directors or members, who are entitled to vote on the resolution;
 - (b) However, if at least 1/3rd of the total number of directors of the company for the time being require that any resolution under circulation must be decided at a meeting, the Chairperson shall put the resolution to be decided at a meeting of the Board (instead of being decided by circulation).
 - (c) A resolution that has been passed by circulation shall have to be necessarily noted in the next meeting of Board or the Committee, as the case may be, and made part of the minutes of such meeting.
2. Under section 173(3) of the Companies Act, 2013 a meeting of the Board shall be called by giving not less than seven days' notice in writing to every director at his address registered with the company and such notice shall be sent by hand delivery or by post or by electronic means.

Section 173(4) further provides that every officer of the company whose duty is to give notice under this section and who fails to do so shall be liable to a penalty of ₹ 25,000.

In the given case, as no notice was served on Mr. P and Mr. Q who are the directors of C-Tech Limited, every officer responsible for such default in serving notice shall be punishable with fine of ₹ 25,000 as required by Section 173 (4).

Neither the Companies Act, 2013 nor the Companies (Meetings of the Board and its Powers) Rules, 2014 lay down any specific provision regarding the validity of a resolution passed by the Board of Directors in case notice was not served to all the directors. The Companies Act, 2013 clearly provide for the notice to be sent to every director. The Supreme Court, in case of *Parmeshwari Prasad vs. Union of India (1974)* has held that the resolutions passed in the board meeting shall not be valid, since notice to all the Directors was not given in writing. Hence, even though the directors concerned knew about the Board meeting, the meeting shall not be valid and resolutions passed thereat also shall not be valid.

3. According to Section 161(2) of the Companies Act, 2013, the Board of Directors of a company may, if so authorised by its articles or by a resolution passed by the company in general meeting, appoint a person, not being a person holding any alternate directorship for any other director in the company or holding directorship in the same company, to act as an alternate director for a director during his absence for a period of not less than three months from India.

According to Section 173(3), a meeting of the Board may be called by giving at least 7 days' notice in writing to every director at his address registered with the company and such notice shall be sent by hand delivery or by post or by electronic means.

There is no legal precedence whether the notice of the meeting is to be sent to the original director or the alternate director. But as a matter of prudence such notice may be served to both the alternate director as well as the original director who is for the time being outside India.

4. Notice of Board meeting

- (i) **Interested director:** Section 173(3) of the Companies Act, 2013 makes it mandatory that every director needs to be given proper notice of every board meeting. It is immaterial whether a director is interested or not. In case of an interested director, notice must be given to him even though in terms of Section 184 (2) he is precluded from participation *i.e.* engaging himself in discussion or voting at the meeting on the business in which he is interested.
- (ii) **A Director who has expressed his inability to attend a particular Board Meeting:** In terms of section 173(3) even if a director states that he will not be able to attend the next Board meeting, notice must be given to that director also.
- (iii) **A director who has gone abroad:** A director who has gone abroad is still a director. Therefore, he is entitled to receive notice of board meetings during his stay abroad.

The Companies Act, 2013, allows delivery of notice of meeting by electronic means also i.e. through e-mail. This factor carries weight because the Companies Act, 2013 permits a director to participate in a meeting by video conferencing or any other audio-visual means also, in addition to physical presence.

5. Under section 179(3) of the Companies Act, 2013, the Board of Directors of a company shall exercise the following powers on behalf of the company by means of resolutions passed at meetings of the Board:

- (a) To make calls on shareholders in respect of money unpaid on their shares;
- (b) To authorise buy-back of securities under section 68;
- (c) To issue securities, including debentures, whether in or outside India;
- (d) To borrow monies;
- (e) To invest the funds of the company;
- (f) To grant loans or give guarantee or provide security in respect of loans;
- (g) To approve financial statement and the Board's report;
- (h) To diversify the business of the company;
- (i) To approve amalgamation, merger or reconstruction;
- (j) To take over a company or acquire a controlling or substantial stake in another company;
- (k) Any other matter which may be prescribed.

Provided that the Board may, by a resolution passed at a meeting, delegate to any Committee of Directors, the Managing Director, the manager or any other principal officer of the company or in the case of a branch office of the company, the principal officer of the branch office, the powers specified in clauses (d) to (f) on such conditions as it may specify.

From the foregoing provisions, it is clear that the Board of MN Limited shall be perfectly in order if it delegates the power to borrow monies under clause (d) of Section 173 (3) to the Managing Director or to the manager or any other principal officer.

6. (i) According to clause (b) of Section 179(3), The Board of Directors of a company shall exercise the power to authorize buy-back of securities under section 68, on behalf of the company by means of resolutions passed at meetings of the Board.

According to Section 68(2), no company shall purchase its own shares or other specified securities, unless—

- (a) the buy-back is authorised by its articles;
- (b) a special resolution has been passed at a general meeting of the company authorising the buy-back:

However, nothing contained in this clause shall apply to a case where—

- (1) the buy-back is, 10% or less of the total paid-up equity capital and free reserves of the company; and
- (2) such buy-back has been authorised by the Board by means of a resolution passed at its meeting,

From the foregoing provisions, it is clear that in case a company, for the first time, resorts to buy-back of its own shares, when the buy-back is limited to 10% of its paid-up share capital, a special resolution will not be required if such buy-back has been authorised by the Board by means of a resolution passed at its meeting. Thus, the Board of Director of Spectra Papers Ltd. is empowered to buy-back the shares because the buy-back is limited to 10% of the paid-up share capital, by means of a resolution passed at the Board meeting.

- (ii) According to clause (e) of Section 179(3), the Board of Directors of a company shall exercise the power to invest the funds of the company, on behalf of the company by means of resolutions passed at the meetings of the Board.

The Board may, under the Proviso to Section 179(3), delegate the power to invest the funds of the company through a board resolution passed at a duly convened Board Meeting. However, the investment in shares of other companies will also be governed by a specific provision contained in Section 186(5), according which no investment shall be made or loan or guarantee or security given by the company unless the resolution sanctioning it is passed at a meeting of the Board with the consent of all the directors present at the meeting and the prior approval of the public financial institution concerned where any term loan is subsisting, is obtained.

Thus, a unanimous resolution of the Board is required. Further, Section 186 does not provide for delegation. Hence, the proposed delegation of power to the Managing Director to invest surplus funds of the company in the shares of some other companies, is not in order.

7. (a) According to Section 177(8) of the Companies Act, 2013, the Board's Report shall, under the provisions of Section 134 (3) which is laid before the general meeting where the financial statements of the company are placed before the members, disclose the composition of the Audit Committee and where the Board has not accepted any recommendations of the Audit Committee, the same shall also be disclosed along with the reasons therefor. Hence, the Board is empowered not to accept the recommendations of the Audit Committee but only under genuine circumstances and supported by legitimate reasons for non-acceptance.

(b) If the Board does not accept the recommendations of the Audit Committee, it shall disclose the same in its report under section 134 (3) which is placed before the general meeting of the company.

8. Under section 177(1) of the Companies Act, 2013 the Board of Directors of every listed public company and such other class or classes of companies, as may be prescribed, shall constitute an Audit Committee. Therefore, MNC Ltd. being a listed company will be bound to constitute an Audit Committee under the Act.

Further under section 177(2) the Audit Committee shall consist of a minimum of three directors with independent directors forming a majority.

Further, majority of the members of Audit Committee including its Chairperson shall be persons with ability to read and understand the financial statement.

The draft Board Resolution for the constitution of an Audit Committee may be as follows:

“Resolved that pursuant to the provision contained in section 177 of the Companies Act 2013 and the applicable clause of Listing Agreement with the Mumbai Stock Exchange, an Audit Committee of the Company be and is hereby constituted with effect from the conclusion of this meeting, with members as under:

1. Mr. A -- An Independent Director.
2. Mr. B -- An Independent Director
3. Mr. C -- An Independent Director
4. Mr. D -- An Independent Director
5. Mr. FE -- Financial Executive
6. Mr. MD -- Managing Director

Further resolved that the Chairman of the Committee, who shall be an Independent Director, be elected by the committee members from amongst themselves.

Further resolved that the quorum for a meeting of the Audit Committee shall be the chairman of the Audit Committee and 2 other members (other than the Managing Director),.

Further resolved that the terms of reference of the Audit Committee shall be in accordance with the provisions of section 177(4) of the Companies Act, 2013.

Further resolved that the Audit committee shall conduct discussions with the auditors periodically about internal control system, the scope of audit including the observations of the auditors.

Further resolved that the Audit Committee shall review the quarterly and annual financial statements and submit the same to the Board with its recommendations, if any.

Further resolved that the recommendations made by the Audit Committee on any matter relating to financial management including the audit report shall be binding on the Board. However, where such recommendations are not accepted by the Board, the reasons for the same shall be recorded in the minutes of the Board meeting and communicated to the shareholders.

Further resolved that the Company Secretary of the Company shall be the Secretary to the Audit Committee.

Further resolved that the Chairman of the Audit Committee shall attend the annual general meeting of the Company to provide any clarifications on matters relating to audit as may be required by the members of the company.

Further resolved that the Board's Report/Annual Report to the members of the Company shall include the particulars of the constitution of the Audit Committee and the details of the non-acceptance of any recommendations of the Audit Committee with reasons therefor."

9. (i) **Borrowing from Financial Institutions:** As per Section 180(1)(c) of the Companies Act, 2013, the Board of Directors of a company, without obtaining the approval of shareholders in a general meeting, can borrow money including moneys already borrowed upto an amount which does not exceed the aggregate of paid up capital of the company, free reserves and securities premium. Such borrowing shall not include temporary loans obtained from the company's bankers in the ordinary course of business. Here, free reserves do not include the reserves set apart for specific purpose.

Since the decision to borrow is to be taken in a meeting to be held on 5th September, 2019, the figures relevant for this purpose are the figures as per the Balance Sheet as at 31.03.2019. According to the above provisions, the Board of Directors of PTL Ltd. can borrow, without obtaining approval of the shareholders in a general meeting, upto an amount calculated as follows:

Particulars	₹
Paid up Capital	75,00,000
General Reserve (being free reserve)	50,00,000
Credit Balance in Profit & Loss Account (to be treated as free reserve)	10,00,000
Debenture Redemption Reserve (This reserve is not to be considered since it is kept apart for specific purpose of debenture redemption)	----
Securities Premium	2,00,000
Aggregate of paid-up capital, free reserves and securities premium	137,00,000
Total borrowing power of the Board of Directors of the company, i.e., 100% of the aggregate of paid-up capital, free reserves and securities premium	137,00,000

Less: Amount already borrowed as secured loans	30,00,000
Amount upto which the Board of Directors can further borrow without the approval of shareholders in a general meeting.	107,00,000

- (ii) **Contribution to Charitable Funds:** As per Section 181 of the Companies Act, 2013, the Board of Directors of a company without obtaining the approval of shareholders in a general meeting, can make contributions to genuine charitable and other funds upto an amount which, in a financial year, does not exceed five per cent of its average net profits during the three financial years immediately preceding, the financial year.

According to the above provisions, the Board of Directors of the PTL Ltd. can make contributions to charitable funds, without obtaining approval of the shareholders in a general meeting, upto an amount calculated as follows:

Net Profit for the year (as calculated in accordance with the provisions of the Companies Act, 2013):

Particulars	₹
For the financial year ended 31.3.2017	12,50,000
For the financial year ended 31.3.2018	19,00,000
For the financial year ended 31.3.2019	<u>34,50,000</u>
TOTAL	<u>66,00,000</u>
Average of net profits during three preceding financial years	<u>22,00,000</u>
Five per cent thereof	<u>1,10,000</u>

Hence, the maximum amount that can be donated by the Board of Directors of PTL Ltd. to a genuine charitable fund during the financial year 2019 -2020 will be limited to ₹ 1,10,000 and the said donation shall not require seeking of approval from the shareholders at a general meeting.

10. **Borrowing by the Company (Section 180 of the Companies Act, 2013):** As per Section 180(1)(c) of the Companies Act, 2013, the Board of Directors of a company, without obtaining the approval of shareholders in a general meeting through a special resolution, can borrow the funds including funds already borrowed upto an amount which does not exceed the aggregate of the paid-up share capital, free reserves and securities premium. Such borrowing shall not include temporary loans obtained from the company's bankers in ordinary course of business.

Free reserves do not include the reserves set apart for specific purpose.

According to the above provisions, the Board of Directors of Prince Company Limited can borrow, without obtaining approval of the shareholders in a general meeting, upto an amount calculated as follows:

Particulars	₹
Paid up Share Capital	40 Crore
General Reserve (being free reserve)	20 Crore
Debenture Redemption Reserve (This reserve is not to be considered since it is kept apart for specific purpose of debenture redemption)	----
Securities Premium	2 Crore
Aggregate of paid-up share capital, free reserve and securities premium	62 Crore
Total borrowing power of the Board of Directors of the company, i.e, 100% of the aggregate of paid-up share capital, free reserves and securities premium	62 Crore
(Less: Amount already borrowed as Long term loan)	<u>(10 Crore)</u>
Amount upto which the Board of Directors can further borrow without the approval of shareholders in a general meeting.	52 Crore

In the present case, the directors of Prince Company Limited by a resolution passed at its meeting have decided to borrow an additional sum of ₹ 90 Crore from the company's bankers. Apparently, the proposed borrowing will be beyond the powers of the Board of Directors.

The management of Prince Company Limited, therefore, should take steps to convene the general meeting and pass a special resolution by the members in the meeting as stated in Section 180(1)(c) of the Companies Act, 2013. Then only, the proposed borrowing of ₹ 90 crore will be valid and binding on the company and its members.

- 11. Powers of Board:** In accordance with the provisions of the Companies Act, 2013, as contained under Section 179(1), the Board of Directors of a company shall be entitled to exercise all such powers and to do all such acts and things, as the company is authorized to exercise and do:

Provided that in exercising such power or doing such act or thing, the Board shall be subject to the provisions contained in that behalf in this Act, or in the memorandum or articles, or in any regulations not inconsistent therewith and duly made thereunder including regulations made by the company in general meeting.

Provided further that the Board shall not exercise any power or do any act or thing which is directed or required, whether under this Act or by the members or articles of the company or otherwise to be exercised or done by the company in general meeting.

Section 180 (1) of the Companies Act, 2013, specifies the powers which the Board of Directors of a company shall exercise only with the consent of the company by a special resolution. Clause (a) of Section 180 (1) defines one such power as the power to sell, lease or otherwise dispose of the whole or substantially the whole of the undertaking of the

company or where the company owns more than one undertaking of the whole or substantially the whole or any of such undertakings.

Therefore, the sale of the undertaking of a company can be made by the Board of Directors only with the consent of members of the company accorded by passing a special resolution.

Even if the power is given to the Board by the memorandum and articles of the company, the sale of the undertaking must be approved by the shareholders in general meeting by passing a special resolution.

Therefore, the correct procedure to be followed is for the Board to approve the sale of the undertaking clearly specifying the terms of such sale and then convene a general meeting of members to have the proposal approved by a special resolution.

In the given case, the procedure followed is completely incorrect and violative of the provisions of the Companies Act, 2013. The shareholders cannot on their own make out a proposal of sale and pass an ordinary resolution to implement it through the directors.

The contention of the shareholders is incorrect in the first place as it is not within their authority to approve a proposal independent of the Board of Directors. It is for the Board to approve a proposal of sale of the undertaking and then let the members to approve it by a special resolution. Accordingly, the contention of the members that they were the principals and the directors as their agents were bound to give effect to the decisions of the members is not correct.

Further, in exercising their powers the directors do not act as agent for the majority of members or even for all the members. The members therefore, cannot by resolution passed by a majority or even unanimously supersede the powers of directors or instruct them how they shall exercise their powers. The shareholders have, however, the power to alter the Articles of Association of the company in the manner they like subject to the provisions of the Companies Act, 2013.

12. (i) Audit Committee – Board's Resolution:

"Resolved that pursuant to Section 177 of the Companies Act, 2013, an Audit Committee consisting of the following Directors be and is hereby constituted.

1. Mr. ---- Independent Director
2. Mr. ---- Independent Director
3. Mr. ----Independent Director
4. Mr. ---- Independent Director
5. Mr. ---- Managing Director.
6. Mr. ---- Chief Financial Officer"

“Further resolved that the Chairman of the Audit Committee shall be elected by its members from amongst themselves and shall be an independent director”.

“Further resolved that the quorum for a meeting of the Audit committee shall be three directors (other than the Managing Director), out of which at least two must be independent directors”.

“Resolved further that the Audit Committee shall perform all the functions as laid down in section 177(4) of the Companies Act, 2013 including but not limited to:

- a. make the recommendation for appointment, remuneration and terms of appointment of the auditors of the company;
- b. review and monitor the independence and performance of auditors of the company and the effectiveness of the audit process”.

“Further resolved that the Audit Committee shall review the quarterly and annual financial statements and submit the same to the Board with its recommendations if any”.

- (ii) Rule 6 of the Companies (Meetings of Board and its Powers) Rules, 2014 states that every listed public company and a company covered under Rule 4 of Companies (Appointment and Qualification of Directors) Rules, 2014 shall constitute an Audit Committee. Rule 4 has prescribed the following classes of companies to constitute an Audit Committee:

- (a) public companies having a paid-up share capital of 10 crore rupees or more;
- (b) public companies having turnover of 100 crore rupees or more;
- (c) public companies which have, in aggregate, outstanding loans, debentures and deposits, exceeding 50 crore rupees.

Hence, in the given case, the likely turnover of R Ltd. shall be ₹ 100 crore or more or capital shall be ₹ 10 crore or more.

- (iii) According to section 177(5), the Audit Committee is empowered to:

- (1) call for the comments of the auditors about:
 - (A) internal control systems,
 - (B) the scope of audit, including the observations of the auditors,
 - (C) review of financial statement before their submission to the Board,
- (2) discuss any related issues with the internal and statutory auditors and the management of the company.

[illegible]

CHAPTER

4

INSPECTION, INQUIRY AND INVESTIGATION



LEARNING OUTCOMES

At the end of this Chapter, you will be able to:

- ❑ Explain the provisions related to Inspection, Inquiry and Investigation
- ❑ Comprehend the Powers of registrars, inspectors and Central Government
- ❑ Describe the Establishment of Serious Frauds Investigation Office and its objectives
- ❑ Define the Duties of directors and other employees during inspection, inquiry and investigation
- ❑ Determine Inspection Report and action to be taken on it, Punishment for contravention or non-compliance based on the Inspection Report.



1. INTRODUCTION

In case of company, Shareholders and Management may be different. The shareholders elect the directors to run the business. The directors are given adequate power to run the affairs of the company. Sometimes there may be abuse of power by directors or officers of company and it may lead to losses for stakeholders. Therefore, it becomes imperative for the Central Government to assume certain powers to investigate into the affairs of the company, particularly where there is reason to believe that the business of the company is being conducted with the intent to defraud its creditors or members or for a fraudulent or unlawful purpose, or in any manner which is oppressive to any of its members. Chapter XIV contains Sections 206 to 229 of the Companies Act, 2013 which deals with the provisions relating to Inspection, Inquiry and Investigation into the affairs of company.

POWERS GIVEN UNDER COMPANIES ACT, 2013

Authorities	Powers
Registrar under sections 206, 207, 208 & 209	Section 206 - Call for information and inspection of books of account, papers and explanations and order for inquiry, Section 207 – Conduct of Inspection and Enquiry, The Registrar have all the powers as are vested in a civil court. Section 208 – Submission of inspection report, Section 209 - Search and seizure,
Inspector under sections 206, 207, 208, 209 & 216	Section 206 - Call for information and inspection of books of account, papers and explanations and order for inquiry, Section 207 – Conduct of Inspection and Enquiry, The Registrar have all the powers as are vested in a civil court. Section 208 – submission of inspection report, Section 209 -Search and seizure Section 216 – To investigate on matters relating to company and its membership for determining ownership of company.
Central Government (CG) under sections 206, 210, 211, 212, 216 & 224	Section 206 – CG may authorize any statutory authority to carry out the Inspection of books of accounts of company, Section 210 - Investigate into affairs of company, Appointment of inspectors to investigate into affairs of the company and to report there on. Section 211 - Establishment of Serious Fraud Investigation Office (SFIO),

	Section 212 - Assignment the investigation into the affairs of company by SFIO Section 216 - Appointment of inspector to investigate on matters relating to company and its membership for determining ownership of company, Section 224 - Actions may be taken in pursuance of inspector's report
Regional director in section 206	Section 206 - Appoint inspector for inspection of books and papers of company
Tribunal under section 213, 221, 222	Section 213 -Pass an order for investigation into company's affairs in other cases, Section 221 - for freezing of assets of company on inquiry and investigation, Section 222 -for imposing restrictions upon securities



2. POWER TO CALL FOR INFORMATION, INSPECT BOOKS AND CONDUCT INQUIRIES (SECTION 206 OF THE COMPANIES ACT, 2013)

Section 206 of the Companies Act, 2013 provides for the power to call for information, inspect books and conduct inquiries.

According to this section:

- (i) **Power of the Registrar to call for information, explanation or documents** [Section 206 (1)]: According to section 206(1) of the Companies Act, 2013, where on scrutiny of any document filed by a company or on any information received by him, the Registrar is of the opinion that any further information or explanation or any further documents relating to the company is necessary, he may by a written notice require the company—
 - (a) to furnish in writing such information or explanation; or
 - (b) to produce such documents, within such reasonable time, as may be specified in the notice.
- (ii) **Duty of the company and its officers** [Section 206 (2)]: On the receipt of a notice under sub-section (1) of section 206, it shall be the duty of the company and its officers concerned to furnish such information or explanation to the best of their knowledge and power and to produce the documents to the Registrar within the time specified or extended by the Registrar

Duty of past officers of the company: According to the proviso to sub-section (2) of section 206, where such information or explanation relates to any past period, the officers who had been in the employment of the company for such period, if so called upon by the Registrar through a notice served on them in writing, shall also furnish such information or explanation to the best of their knowledge.

(iii) **Additional written notice by the Registrar [Section 206 (3)]:** The Registrar may by another written notice call on the company to produce for his inspection such further books of account, books, papers and explanations as he may require at such place and at such time as he may specify in the notice:

- (a) If no information or explanation is furnished to the Registrar within the time specified under Section 206 (1); or
- (b) If the Registrar on an examination of the documents furnished is of the opinion that the information or explanation furnished is inadequate; or
- (c) If the Registrar is satisfied on a scrutiny of the documents furnished that an unsatisfactory state of affairs exists in the company and the information or documents do not disclose a full and fair statement of the information required.

Provided that, before any notice is served under this sub-section, the Registrar shall record his reasons in writing for issuing such notice.

(iv) **Inquiry by the Registrar [Section 206 (4)]:**

- (a) The Registrar may call on the company to furnish in writing any information or explanation on matters specified in the order within such time as he may specify therein and carry out such inquiry as he deems fit after providing the company a reasonable opportunity of being heard, if the Registrar is satisfied:
 - (1) **on the basis of information** available with or furnished to him; or
 - (2) **on a representation** made to him by any a person that the business of a company is being carried on for a fraudulent or unlawful purpose or not in compliance with the provisions of this Act; or
 - (3) the **grievances of investors** are not being addressed,
- (b) Before calling the company to furnish in writing any information or explanations and carrying out the inquiry, the **Registrar has to inform the company of the allegations** made against it by a written order.
- (c) The **Central Government may**, if it is satisfied that the circumstances so warrant, **direct the Registrar or an inspector** appointed by it for the purpose to carry out the inquiry under this sub-section.

- (d) It is further provided that where the business of a company has been or is being carried on for a fraudulent or unlawful purpose, **every officer of the company** who is in default shall be punishable for fraud in the manner as provided in section 447.
- (v) **Inspection by Central Government:** The Central Government may, if it is satisfied that the circumstances so warrant, direct inspection of books and papers of a company by an inspector appointed by it for the purpose [Section 206 (5)].
- (vi) The Central Government may, having regard to the circumstances by general or special order, **authorize any statutory authority to carry out the inspection** of books of account of a company or class of companies [Section 206 (6)].
- (vii) **Failure to furnish information:** If a company fails to furnish any information or explanation or produce any document required under this section, the company and every officer of the company, who is in default shall be punishable with a fine which may extend to 1 lakh rupees and in the case of a continuing failure, with an additional fine which may extend to 500 rupees for every day after the first during which the failure continues [Section 206 (7)].

Note: The said provisions apply to the foreign company also [section 228 of the Companies Act, 2013].

Inquiry under section 206(1) of Companies Act, 2013 is fact finding. It is administrative in nature and it is not necessary to give hearing to the company before ordering inquiry.

Following section can be summarized as;

Concerned authorities	Under the said circumstances	Have following Powers
Power of Registrar to call for information/explanation/production of documents under section 206 (1)	On scrutiny of any document filed by a company or on any information received by him, he is of the opinion that any further information or explanation or any further documents relating to the company is necessary	He may by a written notice require the company— (a) to furnish in writing such information (b) or explanation; or (c) to produce such documents,
Registrar may serve Additional written notice under section 206 (3)	(a) If no information or explanation is furnished, or (b) If on an examination of the documents furnished, he is of the	He may by another written notice call on the company to produce for his inspection such further books of account, books,

	opinion that the information or explanation furnished is inadequate; or (c) If he is satisfied on scrutiny of the documents furnished that an unsatisfactory state of affairs exists in the company and the information or documents do not disclose a full and fair statement of the information required.	papers and explanations as he may required.
Registrar may carry out inquiry under section 206(4)	(1) on the basis of information available with or furnished to him; or (2) on a representation made to him by any person that the business of a company is being carried on for a fraudulent or unlawful purpose or not in compliance with the provisions of this Act; or (3) the grievances of investors are not being addressed,	He may call on the company to furnish in writing any information or explanation on matters specified in the order and carry out such inquiry.
Power of Central Government [Section 206(6)]	if is satisfied that the circumstances so warrant [Section 206 (5)]	It may direct inspection of books and papers of a company by an inspector

		appointed by it for the purpose.
Order passed by Central Government [Section 206(6)]	having regard to the circumstances	By general or special order, authorize any statutory authority to carry out the inspection of books of account of a company or class of companies

1. The High Court of Delhi, in *Axis Ispat (P.) Ltd. v. Union of India*, W.P.(C) No. 4063 of 2021, April 7, 2021 laid down that Registrar of Companies (RoC) has power to call for information, inspection of books, and to conduct an inquiry, however, RoC would have to first call upon company to give an explanation and also provide them a reasonable opportunity of being heard before, issuing show cause notices.

In the given case, RoC by written order sought for inspection of books of account and other statutory records of petitioner company. Petitioner replied to said order belatedly and owing to belated reply, RoC had proceeded further, to issue show cause notice. However, there was a doubt that whether reply submitted by petitioner was considered or not by RoC while issuing show cause notice. In order to ensure that interest of petitioner was properly balanced, and adequate opportunity was afforded to petitioner, RoC was directed to give opportunity of being heard to petitioner and after affording a hearing to petitioner, RoC could proceed further in accordance with law.

2. High Court of Andhra Pradesh and Telangana, in *Karvy Stock Broking Ltd. v. Union of India*, laid down on the Jurisdiction of ROC under section 206(4), is suo motu in nature, because if he is satisfied based on information available with him, or furnished to him, or on a representation by any person that business of company is being carried on for a fraudulent or unlawful purposes, he is empowered to issue notice specifying allegations, and calling upon company to carry out inquiry.

3. CONDUCT OF INSPECTION AND INQUIRY (SECTION 207 OF THE COMPANIES ACT, 2013)

Section 207 of the Companies Act, 2013 provides for the conduct of inspection and inquiry as follows:

- (i) **Duty of director, officer or employee [Sub-Section (1)]**: Where a Registrar or inspector calls for the books of account and other books and papers under sub section (1) of section 206, it shall be the duty of **every director, officer or other employees** of the company:
 - (a) **to produce** all such documents; and

- (b) **to furnish** with such statements, information or explanations in such form as may require; and
- (c) **to render all assistance** in connection with such inspection.

(ii) **Powers of the Registrar or inspector [Sub-section (2) and (3)]:**

- (a) The Registrar or inspector making an inspection or inquiry under section 206 may, during the course of such inspection or inquiry, as the case may be,—
 - (1) make or cause to be made copies of books of account and other books and papers; or
 - (2) place or cause to be placed any marks of identification in such books in token of the inspection having been made.
- (b) The **Registrar or inspector making an inspection or inquiry shall have all the powers as are vested in a civil court** under the Code of Civil Procedure, 1908, while trying a suit in respect of the following matters, namely:—
 - (1) the **discovery and production** of books of account and other documents, at such place and time as may be specified by such Registrar or inspector making the inspection or inquiry;
 - (2) **summoning** and enforcing the attendance of persons and examining them on oath; and
 - (3) **inspection** of any books, registers and other documents of the company at any place.

- (iii) **Penalty for Contravention [sub-section (4)]:** If any director or officer of the company disobeys the direction issued by the Registrar or the inspector under this section, the director or the officer shall be punishable with imprisonment which may extend to 1 year and with fine which shall not be less than 25,000 rupees but which may extend to 1 lakh rupees.

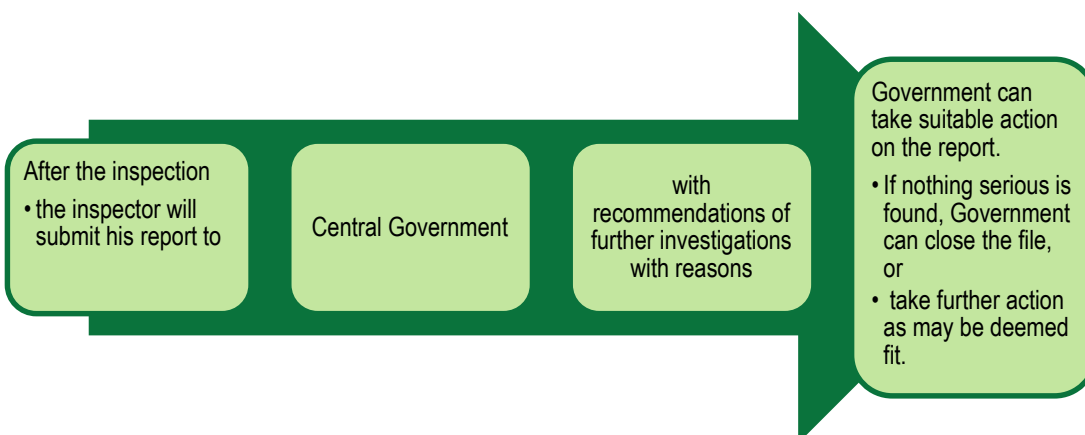
If a director or an officer of the company has been convicted of an offence under this section, the director or the officer shall, on and from the date on which he is so convicted, be deemed to have vacated his office as such and on such vacation of office, shall be disqualified from holding an office in any company.



4. REPORT ON INSPECTION MADE (SECTION 208 OF THE COMPANIES ACT, 2013)

Section 208 of the Companies Act, 2013 provides for the submission of the report on inspection made. According to this section:

The Registrar or inspector shall, after the inspection of the books of account or an inquiry under section 206 and other books and papers of the company under section 207, submit a report in writing to the Central Government. The registrar or inspector may recommend in report that there is the need of further investigation. The said recommendation has to be given with reasons in support.



The said report has to be submitted to Regional Director (RD). [Powers delegated vide Notification F No. 3/76/2015-CL-II dated 31-12-2015]

If the punishment is less than two years, RD himself can sanction launching of prosecution. In other cases, he should forward the report to the Central Government for sanctioning prosecution.

5. SEARCH AND SEIZURE (SECTION 209 OF THE COMPANIES ACT, 2013)

Application to Special Court: Registrar or inspector on reasonable grounds to believe that books and papers relating to the affairs of the company may be destroyed, mutilated, altered, falsified or secreted, he can make an application to Special Court.

Power of special court to search and seize: The Special Court, may, by order, authorize it, to enter into the places or premises where books and papers are placed, to search the place and to seize the books and papers as necessary, after allowing the company to make copies.

Search and seizure must be according to provisions of Code of Criminal Procedure.

Return of seized papers: The seized papers must be returned within 180 days. The Registrar can take copies of any document or place identification marks on them before returning the books and papers. He can ask for the books and papers again, if needed.

According to this section:

(i) **Circumstances for seizure [Sub-section (1)]:** Where, upon information in his possession or otherwise, the Registrar or inspector has reasonable ground to believe that the books and papers of

- (a) a company, or relating to
- (b) the key managerial personnel or
- (c) any director or
- (d) auditor or
- (e) company secretary in practice (if the company has not appointed a company secretary),

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

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

(ii) **Period of seizure [Sub-section (2)]:**

Original period of seizure: The Registrar or inspector **shall return** the books and papers seized under sub-section (1), as soon as may be, and in any case **not later than 180th day after such seizure**, to the company from whose custody or power such books or papers were seized.

Further period of seizure: The books and papers may be called for by the Registrar or inspector for a further period of 180 days by an order in writing if they are needed again.

(iii) **Taking of copies, placing identification marks [second proviso to sub-section (2)]:** The Registrar or inspector may, before returning such books and papers as aforesaid, **take copies of, or extracts from them or place identification marks on them or any part thereof** or deal with the same in such other manner as he considers necessary.

(iv) **Applicability of the provisions of the Code of Criminal Procedure, 1973 [Sub-section (3)]:** The provisions of the Code of Criminal Procedure, 1973 relating to searches or seizures shall apply, mutatis mutandis, to every search and seizure made under this section.

Example 1: A group of creditors of Mac Trading Limited makes a complaint to the Registrar of Companies, Hyderabad alleging that the management of the company is indulging in destruction and falsification of the accounting records of the company. The complainants

requested the Registrar to take immediate steps to seize the records of the company so that the management may not be allowed to tamper with the records.

Here, according to the provisions, Registrar may enter and search the place where such books or papers are kept and seize them **only after obtaining an order** from the Special Court.

Since in the given question, Registrar entered the premises for the search and seizure of books of the company without obtaining an order from the Special Court, it was held that he is not authorized to seize the books of the Mac Trading Limited.

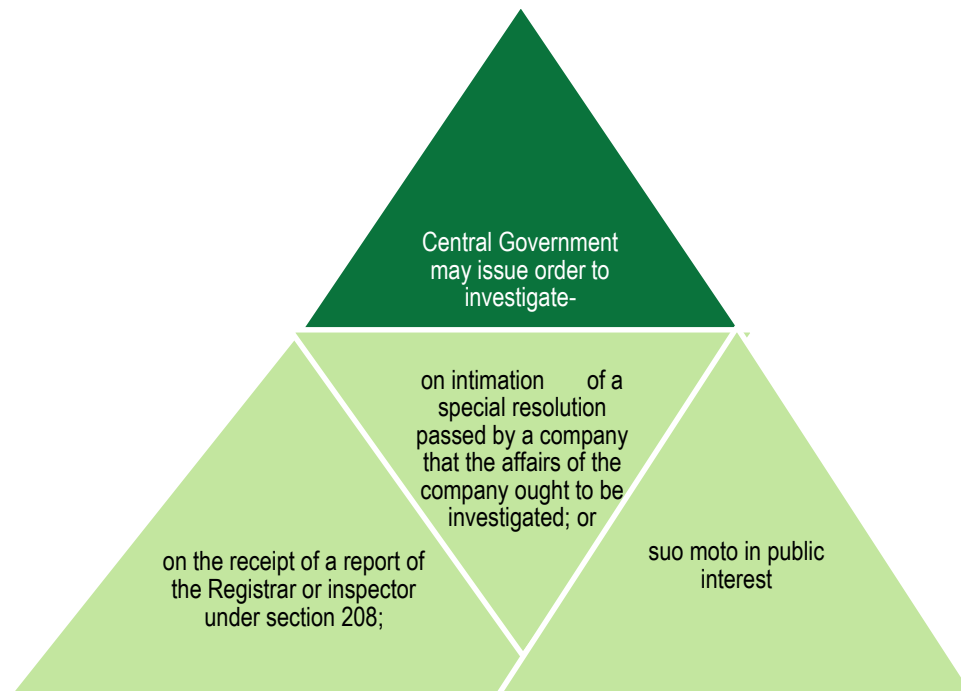


6. INVESTIGATION INTO AFFAIRS OF COMPANY (SECTION 210 OF THE COMPANIES ACT, 2013)

Section 210 of the Companies Act, 2013 provides for Investigation into affairs of company. According to this section:

- (i) **Investigation in the opinion of Central Government** [Sub-section (1)]: Where the Central Government is of the opinion, that it is necessary to investigate into the affairs of a company, it may order an investigation into the affairs of the company.

Central Government may order to investigate-



- (ii) **Investigation on the order by a court or the Tribunal** [Sub-section (2)]: Where an order is passed by a court or the Tribunal in any proceedings before it that the affairs of a company ought to be investigated, the Central Government shall order an investigation into the affairs of that company.
- (iii) **Appointment of inspectors** [Sub-section (3)]: For the purposes of this section, the Central Government may appoint **one or more persons as inspectors** to investigate into the affairs of the company and to report thereon in such manner as the Central Government may direct.

According to the Companies (Inspection, investigation and inquiry) Rules, 2014:

- (i) **Applicant to pay security:** The Central Government may before appointing an inspector under sub-section (3) of Section 210, require the applicant to give a security not exceeding 25,000 rupees for payment of the costs and expenses of investigation as per the criteria given in the said rule.

Sr. No.	Turnover as per previous year balance sheet (₹)	Amount of security (₹)
1	Turnover up to ₹ 50 crore	₹ 10,000
2	Turnover more than ₹ 50 crore and up to 200 crore	₹ 15,000
3	Turnover more than ₹ 200 crore	₹ 25,000

- (ii) **Refund of security to applicant:** Further, the above referred security shall be refunded to the applicant if the investigation results in prosecution.

Example 2: Shareholders of Hide and Seek Ltd. are not satisfied about performance of the company. It is suspected that some activities being run in the name of the company are not in the interest of the company or its members. 101 out of total 500 shareholders of the company have made an application to the Central Government to appoint an inspector to carry out investigation and find out the true picture.

Here, the shareholders' application will not be accepted as under 210 of the Companies Act, 2013, Central Government may order an investigation into affairs of the company on the intimation of a special resolution passed by a company that the affairs of the company ought to be investigated and then may appoint the inspectors. Here, 101 out of total 500 shareholders of the company have made an application to the Central Government to appoint an inspector to carry out investigation but it is not sufficient as the company has not passed the special resolution.



7. ESTABLISHMENT OF SERIOUS FRAUD INVESTIGATION OFFICE (SECTION 211 OF THE COMPANIES ACT, 2013)

Section 211 of the Companies Act, 2013 provides for the establishment of Serious Fraud Investigation Office as under:

- (i) **Setting up of Serious Fraud Investigation Office (SFIO) [Section 211 (1)]:** The Central Government shall, by notification, establish an office to be called the Serious Fraud Investigation Office to investigate frauds relating to a company.
- (ii) **Continuation of earlier SFIO:** Until the SFIO as mentioned above is established, the Serious Fraud Investigation Office set-up by the Central Government in terms of the Government of India Resolution No. 45011/16/2003-Adm-I, dated 2nd July, 2003 shall be deemed to be the Serious Fraud Investigation Office for the purpose of this section.
- (iii) **Composition of SFIO [Section 211 (2)]:** The SFIO shall be:
 - (a) Headed by a **Director**, and
 - (b) Consist of such **number of experts** from the following fields to be appointed by the Central Government from amongst persons of ability, integrity and experience in,—



- (iv) **Appointment of Director** [Section 211 (3)]: The Central Government shall, by notification, **appoint a Director in the SFIO**, who shall be an officer not below the rank of a Joint Secretary to the Government of India having knowledge and experience in dealing with matters relating to corporate affairs.
- (v) **Appointment of Experts Officers & Employees** [Section 211 (4)]: **The Central Government may appoint such experts and other officers and employees** in the SFIO as it considers necessary for the efficient discharge of its functions under this Act.

According to **Rule 3** of the Companies (Inspection, Investigation and Inquiry) Rules, 2014, the Central Government may appoint persons having expertise in the fields of investigations, cyber forensics, financial accounting, management accounting, cost accounting and any other fields as may be necessary for the efficient discharge of Serious Fraud Investigation Office (SFIO) functions under the Act.

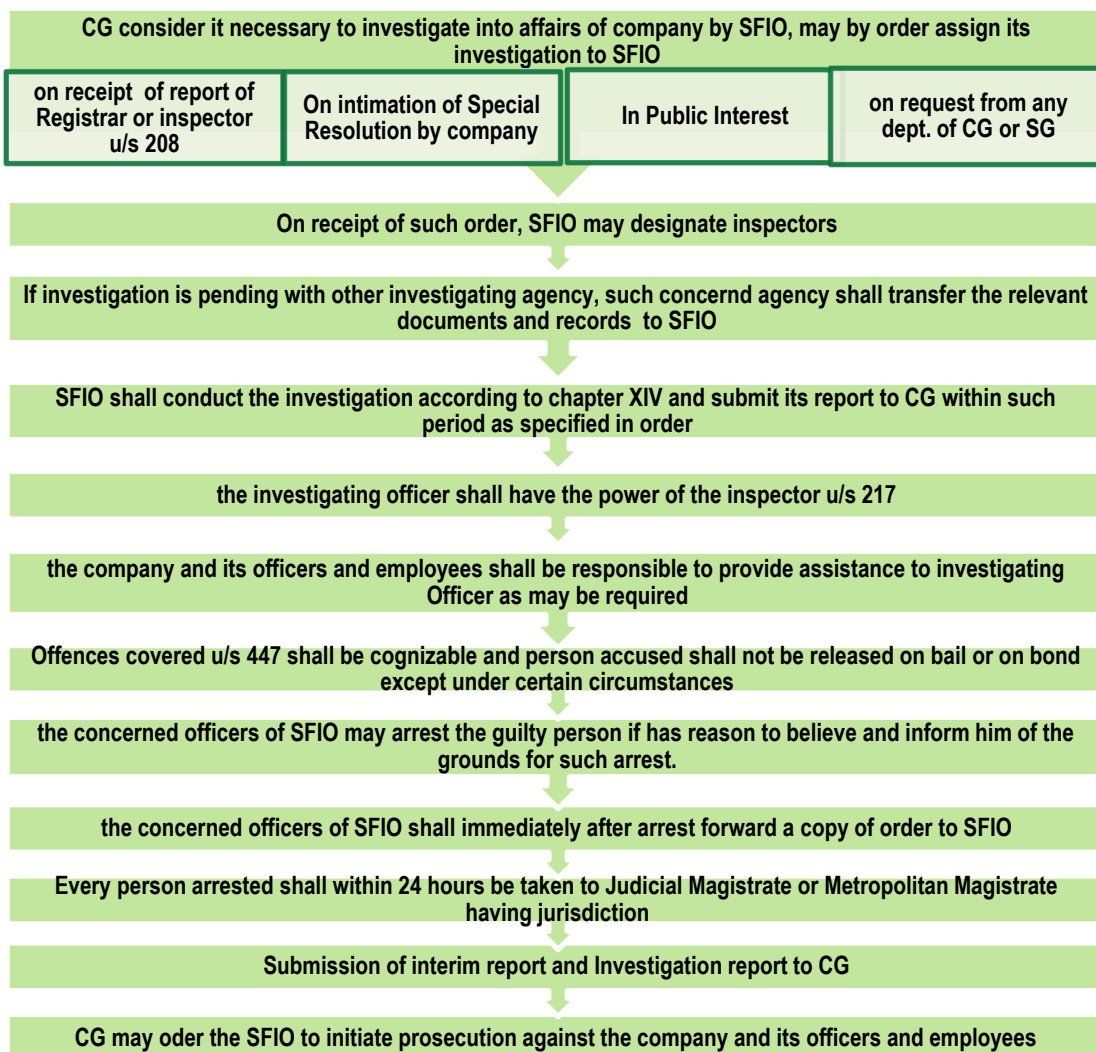
- (vi) **Terms and conditions of service** [Section 211 (5)]: The terms and conditions of service of Director, experts, and other officers and employees of the SFIO shall be such as may be prescribed

The terms and conditions of service of the above mentioned officers have been laid down in the Rule 4 of the Companies (Inspections, Investigations and Inquiry) Rules, 2014.



8. INVESTIGATION INTO AFFAIRS OF COMPANY BY SERIOUS FRAUD INVESTIGATION OFFICE (SECTION 212 OF THE COMPANIES ACT, 2013)

Section 212 of the Companies Act, 2013 provides for Investigation into affairs of Company by the Serious Fraud Investigation Office (SFIO). According to this section:



- (i) **Assigning of investigation to SFIO by CG:** According to section 212(1), where the Central Government -
- on receipt of a report of the Registrar or inspector under section 208;
 - on intimation of a special resolution passed by a company that its affairs are required to be investigated;
 - in the public interest; or
 - on request from any Department of the Central Government or a State Government,

is of the opinion that it is necessary to investigate into the affairs of a company by the SFIO, the Central Government may, by order, assign the investigation into the affairs of the said company to the SFIO.

On receipt of such order, the **Director, SFIO may designate such number of inspectors**, as he may consider necessary for the purpose of such investigation.

- (ii) **No other investigating agency of CG/ or any SG shall proceed with investigation where case is assigned to SFIO:** Where any case has been assigned by the Central Government to the SFIO for investigation under this Act, no other investigating agency of Central Government or any State Government shall proceed with investigation in such case in respect of any offence under this Act. In case any such investigation has already been initiated, it shall not be proceeded further with and the concerned agency shall transfer the relevant documents and records in respect of such offences under this Act to SFIO [Sub section (2)].
- (iii) **Submission of Report to CG:** Where the investigation into the affairs of a company have been assigned by the Central Government to SIFO, it shall conduct the investigation in the manner and follow the procedure provided in this Chapter (Chapter XIV- Inspection, Inquiry and Investigation) and submit its report to the Central Government within such period as may be specified in the order [Sub section (3)]
- (iv) **Investigation by an investigating officer:** The Director, SFIO shall cause the affairs of the company to be investigated by an Investigating Officer who shall have the power of the inspector under section 217 [Sub section (4)]
- (v) **To provide all information, explanation, documents and assistance to the Investigating Officer:** The company and its officers and employees, who are or have been in employment of the company shall be responsible to provide all information, explanation, documents and assistance to the Investigating Officer as he may require for conduct of the investigation [Sub section (5)]
- (vi) **Offences are cognizable and non-Bailable:** As per sub-section (6), offences covered under section 447 of this Act shall be cognizable and no person accused of any offence under those sections shall be released on bail or on his own bond unless—
 - (a) the Public Prosecutor has been given an opportunity to oppose the application for such release; and
 - (b) where the Public Prosecutor opposes the application, the court is satisfied that there are reasonable grounds for believing that he is not guilty of such offence and that he is not likely to commit any offence while on bail.

However, a person, who, is

- (a) under the age of sixteen years or
- (b) is a woman or

(c) is sick or infirm,

may be released on bail, if the Special Court so directs.

Provided further that the Special Court shall not take cognizance of any offence referred in point (vi) above except upon a complaint in writing made by—

(a) the Director, SFIO; or

(b) any officer of the Central Government authorised, by a general or special order in writing in this behalf by that Government.

(vii) **Granting of Bail:** The limitation on granting of bail specified in sub section (6) above is in addition to the limitations under the Code of Criminal Procedure, 1973 or any other law for the time being in force on granting of bail [Sub section (7)].

(viii) **Power to arrest:** If any officer not below the rank of Assistant Director of SFIO authorized in this behalf by the Central Government by general or special order, has on the basis of material in his possession reason to believe (the reason for such belief to be recorded in writing) that any person has been guilty of any offence punishable under sections referred to in sub-section (6), he may arrest such person and shall, as soon as may be, inform him of the grounds for such arrest. [Sub section (8)]

(ix) **Forward copy of order to SFIO:** The officer authorized under sub-section (8) shall, immediately after arrest of such person under such sub-section(8), forward a copy of the order, along with the material in his possession, referred to in that sub-section, to the SFIO in a sealed envelope, in such manner as may be prescribed and the SFIO shall keep such order and material for such period as may be prescribed. [Sub section (9)]

(x) **Presented before Special Court/JM/MM:** Every person arrested under sub-section (8) shall within **twenty-four hours**, be taken to a Special Court or Judicial Magistrate, or a Metropolitan Magistrate as the case may be, having jurisdiction.

The period of twenty-four hours shall exclude the time necessary for the journey from the place of arrest to the Special Court or Magistrate's court. [Sub section (10)]

(xi) **Submission of Interim Report to CG:** The SFIO shall submit an interim report to the Central Government, if the Central Government so directs [Sub section (11)].

(xii) **Submission of investigation report to CG:** The SFIO shall submit the investigation report to the Central Government on completion of the investigation [sub section (12)].

(xiii) **Receiving of copy of the investigation report by making an application to the court:** Notwithstanding anything contained in this Act or in any other law for the time being in force, a copy of the investigation report may be obtained by any person concerned by making an application in this regard to the court [Sub section (13)].

- (xiv) **CG may direct SFIO to initiate prosecution:** On receipt of the investigation report, the Central Government may, after examination of the report (and after taking such legal advice, as it may think fit), direct the SFIO to initiate prosecution against the company and its officers or employees, who are or have been in employment of the company or any other person directly or indirectly connected with the affairs of the company [Sub section (14)].

(14A) **Where report mentions fraud has taken place:** Where the report under sub-section (11) or sub-section (12) states that fraud has taken place in a company and due to such fraud, any director, key managerial personnel, other officer of the company or any other person or entity, has taken undue advantage or benefit, whether in the form of any asset, property or cash or in any other manner, the Central Government may file an application before the Tribunal for appropriate orders with regard to disgorgement of such asset, property or cash and also for holding such director, key managerial personnel, other officer or any other person liable personally without any limitation of liability.

Example 3– Mr. A a director of Pappu Ltd., received a car in gift from his supplier for giving him order in bulk quantity with higher rate than market. This fact was reported in the investigation report under sub-section (11) or sub-section (12), there CG may file an application before the Tribunal for appropriate orders to recover this car from Mr. A.

- (xv) **Filing of investigation Report with the special court:** Notwithstanding anything contained in this Act or in any other law for the time being in force, the investigation report filed with the Special Court for framing of charges shall be deemed to be a report filed by a police officer under section 173 of the Code of Criminal Procedure, 1973 [Sub section (15)].
- (xvi) **Investigation/action conducted under Companies Act, 1956:** Notwithstanding anything contained in this Act, any investigation or other action taken or initiated by SFIO under the provisions of the Companies Act, 1956 shall continue to be proceeded with under that Act as if this Act had not been passed [Sub section (16)].
- (xvii) **Providing of all information/documents to SFIO:** In case SFIO has been investigating any offence under this Act, any other investigating agency, State Government, police authority, income-tax authorities having any information or documents in respect of such offence shall provide all such information or documents available with it to the SFIO [Sub section (17) (a)].
- (xviii) **Sharing of information by SFIO:** The SFIO shall share any information or documents available with it, with any investigating agency, State Government, police authority or income tax authorities, which may be relevant or useful for such investigating agency, State Government, police authority or income-tax authorities in respect of any offence or matter being investigated or examined by it under any other law [Sub section (17) (b)].

Note: According to the Companies (Arrests in Connection with Investigation by Serious Fraud Investigation Office) Rules, 2017 vide Notification G.S.R. 1062(E) dated 24th of August 2017, where any person has been guilty of any offence punishable under section 212 of the Act, he may be arrested as per the respective rules.

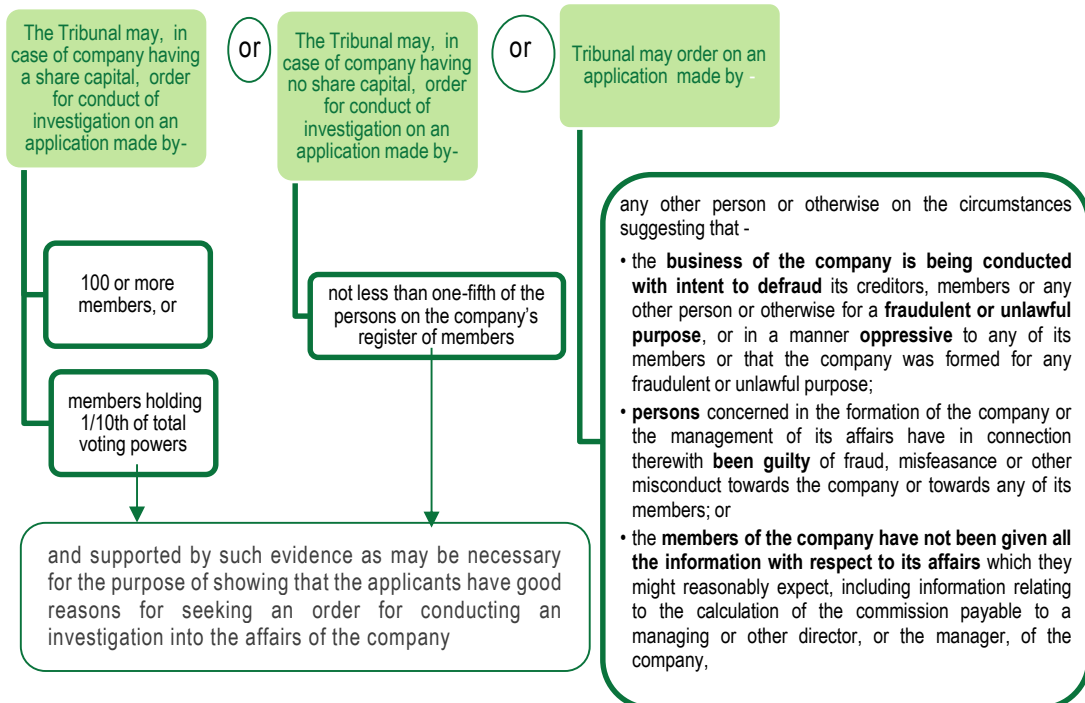
High Court of Andhra Pradesh and Telangana, in *Karvy Stock Broking Ltd. v. Union of India*, held that Section 212(2) mandates that where any case has been assigned by Central Government to SFIO for investigation under Companies Act, no other investigating agency of Central Government or State Government shall proceed with investigation in such case in respect of any offence under this Act.



9. INVESTIGATION INTO COMPANY'S AFFAIRS IN OTHER CASES (SECTION 213 OF THE COMPANIES ACT, 2013)

Section 213 deals with the Investigation into Company's Affairs in other cases. According to this section, NCLT can order investigation in specified cases. Such order can be passed by NCLT only after giving reasonable opportunity of being heard to the concerned parties.

Cognizance of offence by Tribunal:



After giving a reasonable opportunity of being heard to the parties concerned, that the affairs of the company ought to be investigated by an inspector/s appointed by the Central Government and where such an order is passed by the Tribunal, the Central Government shall appoint one or more competent persons as inspectors to investigate into the affairs of the company in respect of such matters and to report thereupon to it in such manner as the Central Government may direct.

Punishment in case of guilty: If after investigation, it is proved that—

- (i) the business of the company is being **conducted with intent to defraud** its creditors, members or any other persons or otherwise for a **fraudulent or unlawful purpose**, or that the company was formed for any fraudulent or unlawful purpose; or
- (ii) any person concerned in the formation of the company or the management of its affairs have in connection therewith been **guilty of fraud**,

then-

- (a) **every officer** of the company who is in default, and
- (b) **the person or persons concerned in the formation of the company or the management of its affairs** shall be punishable for fraud in the manner as provided in section 447.



10. SECURITY FOR PAYMENT OF COSTS AND EXPENSES OF INVESTIGATION (SECTION 214 OF THE COMPANIES ACT, 2013)

Section 214 of the Companies Act, 2013 provides for security for payment of costs and expenses of investigation as under:

Where an investigation is:

- (i) **ordered by the Central Government** in pursuance of clause (b) of sub-section (1) of section 210, or
- (ii) **made by the Tribunal** under section 213,

the **Central Government may before appointing an inspector** under sub-section (3) of section 210 or clause (b) of section 213, require **the applicant to give such security not exceeding 25,000 rupees** as may be prescribed¹, as it may think fit, for payment of the costs and expenses of the investigation.

¹See rule 5 of the Companies (Inspection, Investigation & Inquiry) Rules, 2014

Such security shall be **refunded** to the applicant if the investigation results in prosecution.



11. FIRM, BODY CORPORATE OR ASSOCIATION NOT TO BE APPOINTED AS INSPECTOR (SECTION 215 OF THE COMPANIES ACT, 2013)

Section 215 of the Companies Act, 2013 provides that no **firm, body corporate or other association** shall be appointed as an inspector.



12. INVESTIGATION OF OWNERSHIP OF COMPANY (SECTION 216 OF THE COMPANIES ACT, 2013)

Section 216 of the Companies Act, 2013 provides for Investigation of ownership of company. Central Government can order investigation into ownership to decide who are financially interested and who are in real control of the company. According to the section-

- (i) **Appointment of inspectors by CG:** where it appears to the Central Government that there is a reason so to do, it may appoint one or more inspectors to investigate and report on matters relating to the company, and its membership for the purpose of determining the true persons—
 - (a) who are or have been **financially interested** in the success or failure, whether real or apparent, of the company; or
 - (b) who are or have been able to **control or to materially influence the policy** of the company, or
 - (c) who have or had **beneficial interest in shares** of a company or who are or have been **beneficial owners** or significant beneficial owner of a company. [Sub-section (1)]
- (ii) **Appointment of inspectors by CG where Tribunal directs for investigation:** the Central Government shall appoint one or more inspectors, if the Tribunal, in the course of any proceeding before it, directs by an order that the affairs of the company ought to be investigated as regards the membership of the company and other matters relating to the company, for the purposes specified in sub-section (1) [Sub-section (2)]
- (iii) **To define scope of investigation while appointing an inspector:** While appointing an inspector under sub-section (1), the Central Government may define the scope of the investigation, whether as respects the matters or the period to which it is to extend or otherwise, and in particular, may limit the investigation to matters connected with particular shares or debentures [Sub-section (3)]
- (iv) **Power of Inspector:** Subject to the terms of appointment of an inspector, his powers shall extend

to the investigation of any circumstances suggesting the existence of any arrangement or understanding which, though not legally binding, is or was observed or is likely to be observed in practice and which is relevant for the purposes of his investigation [Sub-section (4)]

Imposition on restrictions during investigation on securities issued or to be issued by company - During investigation under section 216, NCLT can impose certain restrictions upon securities. Such restriction can be upto three years [section 222(1) of Companies Act, 2013].

If despite such order, there is issue or transfer of securities, company as well as every officer who is in default is liable for punishment of fine and imprisonment [section 222(2) of Companies Act, 2013]

Applicability of provisions to foreign company - The provisions of investigation of ownership apply to foreign company also [section 228 of Companies Act, 2013]



13. PROCEDURE, POWERS, ETC., OF INSPECTORS (SECTION 217 OF THE COMPANIES ACT, 2013)

Section 217 of the Companies Act, 2013 provides for procedure, powers, etc., of inspectors as under:

- (i) **Duty of all officers and other employees and agents including former officers, employees and agents:** As per sub- section (1), it shall be the duty of all officers and other employees and agents including the former officers, employees and agents of a company **which is under investigation** in accordance with the provisions contained in this Chapter, and where the affairs of any other body corporate or a person are investigated under section 219, of all officers and other employees and agents including former officers, employees and agents of such body corporate or a person—
 - (a) to **preserve and to produce** to an inspector or any person authorised by him in this behalf all books and papers of, or relating to, the company or, as the case may be, relating to the other body corporate or the person, which are in their custody or power; and
 - (b) otherwise to give to the inspector **all assistance** in connection with the investigation which they are reasonably able to give.
- (ii) **The inspector may require any body corporate, other than a body corporate referred in point (i)** to furnish such information to, or produce such books and papers before him or any person authorized by him in this behalf as he may consider necessary, if the furnishing of such information or the production of such books and papers is relevant or necessary for the purposes of his investigation [Sub section (2)].

- (iii) **Period of custody of inspector:** The inspector shall not keep in his **custody** any books and papers produced under point (i) or point (ii) above for **more than 180 days** and return the same to the company, body corporate, firm or individual by whom or on whose behalf the books and papers were produced [Sub section (3)].

However, the books and papers may be called for by the inspector if they are **needed again** for a **further period of 180 days** by an order in writing.

- (iv) **Examination on oath:** As per sub-section (4), an inspector may **examine on oath**—

- (a) **any of the persons** referred to in point (i); and
- (b) any other person with the **prior approval of the Central Government**,

in relation to the affairs of the company, or other body corporate or person, as the case may be, and for that purpose **may require** any of those persons **to appear before him personally**.

However, in case of an investigation under section 212, the prior approval of Director, SFIO shall be sufficient under point (b) above (instead of the Central Government).

- (v) **Powers to inspectors similar as are vested in a civil court:** As per sub-section (5), notwithstanding anything contained in any other law for the time being in force or in any contract to the contrary, the **inspector**, being an officer of the Central Government making an investigation under this chapter, **shall have all the powers as are vested in a civil court** under the Code of Civil Procedure, 1908, while trying a suit in respect of the following matters, namely:—

- (a) the **discovery and production** of books of account and other documents, at such place and time as may be specified by such person;
- (b) **summoning** and enforcing the attendance of persons and **examining them on oath**; and
- (c) **inspection** of any books, registers and other documents of the company at any place.

- (vi) **Punishment:** If any director or officer of the company **disobeys the direction** issued by the Registrar or the inspector under this section, the director or the officer shall be punishable with imprisonment which may extend to one year and with fine which shall not be less than 25,000 rupees but which may extend to 1 lakh rupees [Sub section (6) (i)].

On Conviction: If a director or an officer of the company has been convicted of an offence under this section, the director or the officer shall, on and from the date on which he is so convicted, be deemed to have vacated his office as such and on such vacation of office, shall be disqualified from holding an office in any company [Sub section (6) (ii)].

- (vii) The **notes of any examination** under sub section (4) above, shall be taken down in **writing** and shall be **read over** to, or by, and **signed by**, the person examined, and may thereafter be **used in evidence** against him [Sub section (7)].
- (viii) **In case of failure /refusal to produce, furnish, appear and sign** : As per sub-section (8), if any person **fails** without reasonable cause or **refuses**—
- to produce** to an inspector or any person authorised by him in this behalf any book or paper which is his duty under point (i) or point (ii) to produce;
 - to furnish any information** which is his duty under point (ii) to furnish;
 - to appear before the inspector personally** when required to do so under point (iv) or **to answer any question** which is put to him by the inspector in pursuance of that point; or
 - to sign the notes** of any examination referred to in sub section (7) above,
- he shall be punishable with imprisonment for a term which may extend to 6 months and with fine which shall not be less than 25,000 rupees but which may extend to 1 lakh rupees, and also with a further fine which may extend to 2,000 rupees for every day after the first during which the failure or refusal continues.
- (ix) **Providing of assistance to the inspector**: The officers of the Central Government, State Government, police or statutory authority shall provide **assistance to the inspector** for the purpose of inspection, inquiry or investigation, which the inspector may, with the prior approval of the Central Government, require [Sub section (9)].
- (x) **Provision for reciprocal arrangements**: The Central Government may enter into an **agreement with the Government of a foreign State for reciprocal arrangements** to assist in any inspection, inquiry or investigation under this Act or under the corresponding law in force in that State and may, by notification, render the application of this Chapter in relation to a foreign State with which reciprocal arrangements have been made subject to such modifications, exceptions, conditions and qualifications as may be deemed expedient for implementing the agreement with that State [Sub section (10)].
- (xi) **Issue of letter of request where evidence is, or may be, available in a country or place outside India by competent court**: Notwithstanding anything contained in this Act or in the Code of Criminal Procedure, 1973 if, in the course of an investigation into the affairs of the company, an application is made to the competent court in India by the **inspector stating that evidence is, or may be, available in a country or place outside India**, such court may issue a letter of request to a court or an authority in such country or place, competent to deal with such request, to examine orally, or otherwise, any person, supposed to be acquainted with the facts and circumstances of the case, to record his statement made in the course of

such examination and also to require such person or any other person to produce any document or thing, which may be in his possession pertaining to the case, and to forward all the evidence so taken or collected or the authenticated copies thereof or the things so collected to the court in India which had issued such letter of request [Sub section (11)].

Provided that, the letter of request shall be transmitted in such manner as the Central Government may specify in this behalf.

Provided further that every statement recorded or document or thing received under this sub-section shall be deemed to be the evidence collected during the course of investigation.

According to Rule 6 of the Companies (Inspection, investigation and inquiry) Rules, 2014, the 'letter of request', in terms of section 217, shall be transmitted in such manner as specified by the Ministry of Corporate Affairs.

- (xii) **Upon receipt of a letter of request** from a court or an authority in a country or place outside India, competent to issue such letter in that country or place for the examination of any person or production of any document or thing in relation to affairs of a company under investigation in that country or place, the **Central Government may, if it thinks fit, forward such letter of request to the court concerned**, which shall thereupon summon the person before it and record his statement or cause any document or thing to be produced, or send the letter to any inspector for investigation, who shall thereupon investigate into the affairs of company in the same manner as the affairs of a company are investigated under this Act and the inspector shall submit the report to such court **within 30 days or such extended time** as the court may allow for further action [Sub section (12)].

Provided that the **evidence taken or collected as above or authenticated copies thereof or the things so collected shall be forwarded by the court, to the Central Government for transmission**, in such manner as the Central Government may deem fit, to the court or the authority in country or place outside India which had issued the letter of request.

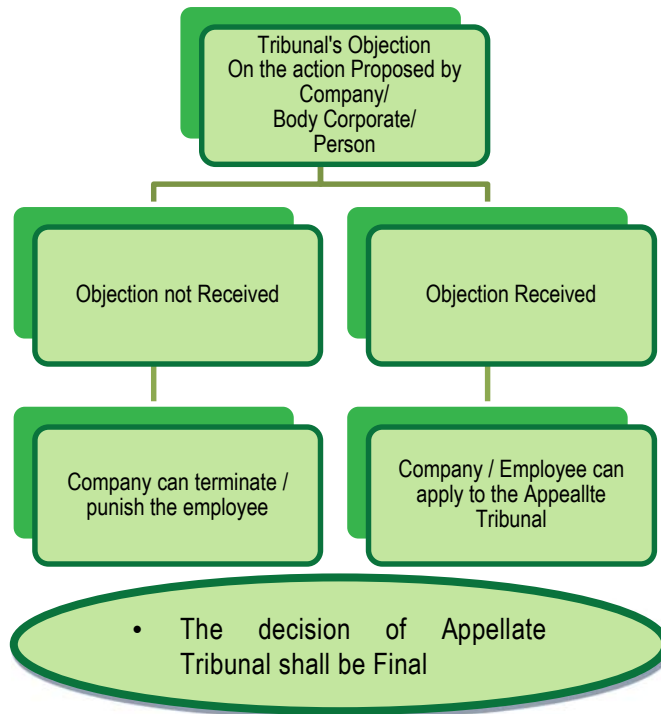


14. PROTECTION OF EMPLOYEES DURING INVESTIGATION (SECTION 218 OF THE COMPANIES ACT, 2013)

Section 218 of the Act deals with the protection of Employees during Investigation. An employee of company who has disclosed information during investigation is protected against dismissal, discharge or removal or change in terms of his employment to his disadvantage, during investigation, without permission of NCLT.

- (1) **Approval of tribunal to take action against the employee:** Notwithstanding anything contained in any other law for the time being in force, if—
- (a) **during the course of any investigation of the affairs** and other matters of or relating to a company, other body corporate or person under section 210, section 212, section 213 or section 219 or of the membership and other matters of or relating to a company, or the ownership of shares in or debentures of a company or body corporate, or the affairs and other matters of or relating to a company, other body corporate or person, under section 216; or
 - (b) **during the pendency of any proceeding** against any person concerned in the conduct and management of the affairs of a company under Chapter XVI, such company, other body corporate or person proposes—
 - (i) to discharge or suspend any employee; or
 - (ii) to punish him, whether by dismissal, removal, reduction in rank or otherwise; or
 - (iii) to change the terms of employment to his disadvantage,
- the company, other body corporate or person, as the case may be, **shall obtain approval of the Tribunal of the action proposed** against the employee and **if the Tribunal has any objection to the action proposed**, it shall send by post notice thereof in writing to the company, other body corporate or person concerned.
- (2) **Action against employee:** If the company, other body corporate or person concerned does **not** receive **within thirty days** of making of application under sub-section (1), **the approval of the Tribunal**, then and only then, the company, other body corporate or person concerned may proceed to take against the employee, the action proposed.
- (3) **Appeal:** If the company, other body corporate or person concerned is **dissatisfied with the objection raised by the Tribunal**, it may, within a period of thirty days of the receipt of the notice of the objection, **prefer an appeal to the Appellate Tribunal** in such manner and on payment of such fees as may be prescribed.
- (4) **Final and Binding order:** The decision of the Appellate Tribunal on such appeal shall be **final and binding** on the Tribunal and on the company, other body corporate or person concerned.

- (5) **Over-riding effect:** For the removal of doubts, it is hereby declared that the provisions of this section shall have effect without prejudice to the provisions of any other law for the time being in force.



15. POWERS OF INSPECTOR

1. To conduct investigation into affairs of related companies, etc. (Section 219 of the Companies Act, 2013)

Section 219 of the Companies Act, 2013 provides for power of inspector to conduct investigation into affairs of related companies, etc. as under:

Investigation into affairs of related companies: If an inspector appointed under section 210 or section 212 or section 213 to investigate into the affairs of a company considers it necessary for the purposes of the investigation, can also investigate the affairs of—

any other body corporate which is, or has at any relevant time been the **company's subsidiary company or holding company, or a subsidiary company of its holding company;**

any other body corporate which is, or has at any relevant time **been managed by any person as managing director or as manager**, who is, or was, at the relevant time, the managing director or the manager of the company;

any other body corporate whose **Board of Directors comprises nominees of the company** or is accustomed to **act in accordance with the directions or instructions of the company or any of its directors;** or

any person who is or has at any relevant time **been the company's managing director or manager or employee.**

Report of inspector: The inspector shall, subject to the prior approval of the Central Government, investigate into and report on the affairs of the other body corporate or of the managing director or manager, in so far as he considers that the results of his investigation are relevant to the investigation of the affairs of the company for which he is appointed.

The Supreme Court of India in *Serious Fraud Investigation Office v. Sahara Housing Investment Corporation Ltd.* passed an order under section 212, read with section 219, of the Companies Act, 2013. Serious Fraud Investigation Office in Investigation with regard to construction of section 212(3) statute it was held that it does not contain any specific prescription of time and reference to completion of investigation within a stipulated period is directory and not mandatory.

On basis of a report submitted by RoC, Government of India in Ministry of Corporate Affairs passed an order directing SFIO to investigate into affairs of several corporate entities in Sahara group and furnish a report within a period of three months therefrom. High Court by impugned order stayed operation and implementation of said order on ground that SFIO was unable to complete investigation within stipulated time and, thus, there was violation of section 212(3) and direction of Central Government. It was held that Union Government was only ordering an investigation and it would be inappropriate to place a burden of recording elaborate reasons when purpose of investigation was to ensure that a full enquiry into affairs of companies was carried out.

2. Seizure of documents by inspector (Section 220 of the Companies Act, 2013)

Section 220 of the Companies Act, 2013 provides for seizure of documents by inspector as under:

- (i) **Seizure of books and papers [Sub section (1)]:** Where in the course of an investigation under this Chapter, the inspector has reasonable grounds to believe that the books and

papers of, or relating to, any company or other body corporate or managing director or manager of such company are likely to be **destroyed, mutilated, altered, falsified or secreted**, the inspector may—

- (a) **enter**, with such assistance as may be required, the place or places where such books and papers are kept in such manner as may be required; and
 - (b) **seize** books and papers as he considers necessary after allowing the company to take copies of, or extracts from, such books and papers at its cost for the purposes of his investigation.
- (ii) **Time period for keeping books and papers [Sub section (2)]:** The inspector shall keep in his custody the books and papers seized under this section for such a **period not later than the conclusion of the investigation** as he considers necessary and thereafter **shall return** the same to the company or the other body corporate, or, as the case may be, to the managing director or the manager or any other person from whose custody or power they were seized.
- (iii) **Extracts of books and papers:** The inspector may, before returning such books and papers as aforesaid, take copies of, or extracts from them or place identification marks on them or any part thereof or deal with the same in such manner as he considers necessary.
- (iv) **Application of provisions of Cr.PC.:** The provisions of the Code of Criminal Procedure, 1973, relating to searches or seizures shall apply *mutatis mutandis* to every search or seizure made under this section.



16. POWERS OF TRIBUNAL

1. Freezing of Assets of Company on Inquiry and Investigation (Section 221 of the Companies Act, 2013)

Section 221 of the Act deals with the Freezing of Assets of Company on Inquiry and Investigation. Central Government can make application to NCLT for freezing of assets, funds and properties of the company, if there is reasonable ground to believe that removal or transfer or disposal of funds, assets or properties of company is likely to take place in manner prejudicial to interests of company or its shareholders or creditors or in public interest.

According to this section:

- (i) **Order of the tribunal:** Where it appears to the Tribunal,
 - (a) **on a reference made to it by the Central Government** or in connection with any inquiry or investigation into the affairs of a company under this Chapter or
 - (b) **on any complaint** made by such number of **members** as specified under sub-section (1) of section 244 or

- (c) **a creditor** having one lakh amount outstanding against the company or
- (d) **any other person** having a reasonable ground to believe that the removal, transfer or disposal of funds, assets, properties of the company is likely to take place in a manner that is prejudicial to the interests of the company or its shareholders or creditors or in public interest,

it may by order direct that such transfer, removal or disposal shall not take place during such period **not exceeding three years** as may be specified in the order or may take place subject to such conditions and restrictions as the Tribunal may deem fit.

- (ii) **Punishment in case of contravention of order of tribunal:** In case of any removal, transfer or disposal of funds, assets, or properties of the company in contravention of the order of the Tribunal under sub-section (1), the company shall be
 - (a) **punishable with fine** which shall not be less than one lakh rupees but which may extend to twenty-five lakh rupees and
 - (b) **every officer of the company** who is in default shall be punishable with imprisonment for a term which may extend to three years or with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees, or with both.

2. Imposition of Restrictions upon Securities (Section 222 of the Companies Act, 2013)

Section 222 of the Act deals with the Imposition of Restrictions upon Securities. According to this section:

- (i) **Tribunal may by order put restrictions upon securities:** Where it appears to the **Tribunal**, in connection with any investigation under section 216 or **on a complaint made by any person** in this behalf, that there is good reason to find out the relevant facts about any securities issued or to be issued by a company and the Tribunal is of the opinion that such facts cannot be found out unless certain restrictions, as it may deem fit, are imposed, the Tribunal may, by order, direct that the securities shall be subject to such restrictions as it may deem fit for such period not exceeding three years as may be specified in the order.
- (ii) **Punishment in case of contravention to an order:** Where securities in any company are issued or transferred or acted upon in contravention of an order of the Tribunal under sub-section (1),
 - (a) the company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to twenty-five lakh rupees and
 - (b) every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees, or with both.



17. INSPECTOR'S REPORT (SECTION 223 OF THE COMPANIES ACT, 2013)

Section 223 of the Companies Act, 2013 lays down the following provisions in respect of the Inspector's report on investigation conducted under this chapter:

- (i) **Submission of interim report and final report [Sub section (1)]:** An inspector appointed under this Chapter (Chapter XIV- Inspection, Inquiry and Investigation) may, and if so directed by the Central Government shall, submit interim reports to that Government, and on the conclusion of the investigation, shall submit a final report to the Central Government.
- (ii) **Report to be in writing or printed [Sub section (2)]:** Every report made under sub section (1) above, shall be in writing or printed as the Central Government may direct.
- (iii) **Obtaining copy or report [Sub section (3)]:** A copy of the above report may be obtained by members, creditors or any other person whose interest is likely to be affected by making an application in this regard to the Central Government.
- (iv) **Authentication of report [Sub section (4)]:** The report of any inspector appointed under this Chapter shall be authenticated either—
 - (a) by the seal, if any, of the company whose affairs have been investigated; or
 - (b) by a certificate of a public officer having the custody of the report, as provided under section 76 of the Indian Evidence Act, 1872,

and such report shall be admissible in any legal proceeding as evidence in relation to any matter contained in the report.

- (v) **Exceptions [Sub section (5)]:** Nothing in this section shall apply to the report referred to in section 212 of the Companies Act, 2013.



18. ACTIONS TO BE TAKEN IN PURSUANCE OF INSPECTOR'S REPORT (SECTION 224 OF THE COMPANIES ACT, 2013)

Section 224 of the Companies Act, 2013 provides the following provisions in respect of the actions to be taken in pursuance of inspector's report:

- (i) **On basis of report , if person appears to be guilty of offence:** If, from an inspector's report, made under section 223, it appears to the Central Government that any person has, in relation to the company or in relation to any other body corporate or other person whose

affairs have been investigated under this Chapter been guilty of any offence for which he is criminally liable, the Central Government may prosecute such person for the offence and it shall be the duty of all officers and other employees of the company or body corporate to give the Central Government the necessary assistance in connection with the prosecution [Sub section (1)].

- (ii) **Filing of petition by person authorized by the Central Government:** As per sub-section (2), if any company or other body corporate is liable to be wound up under this Act or under the Insolvency and Bankruptcy Code, 2016 and it appears to the Central Government from any such report made under section 223 that it is expedient so to do by reason of any such circumstances as are referred to in section 213, the Central Government may, unless the company or body corporate is already being wound up by the Tribunal, cause to be presented to the Tribunal by any person authorized by the Central Government in this behalf—
 - (a) a petition for the winding up of the company or body corporate on the ground that it is just and equitable that it should be wound up;
 - (b) an application under section 241; or
 - (c) both.
- (iii) **Initiation of winding up proceeding suo moto by the Central Government:** As per sub-section (3), if from any such report as aforesaid, it appears to the Central Government that proceedings ought, in the public interest, to be brought by the company or any body corporate whose affairs have been investigated under this Chapter—
 - (a) for the **recovery of damages** in respect of any fraud, misfeasance or other misconduct in connection with the promotion or formation, or the management of the affairs, of such company or body corporate; or
 - (b) for the **recovery of any property** of such company or body corporate which has been misapplied or wrongfully retained,

the Central Government may itself bring proceedings for winding up in the name of such company or body corporate.
- (iv) **Indemnification to the Central Government:** The Central Government, shall be indemnified by such company or body corporate against any costs or expenses incurred by it in, or in connection with, any proceedings brought by virtue of sub-section (3) [Sub section (4)].
- (v) **Where fraud has been committed:** Where the report made by an inspector states that fraud has taken place in a company and due to such fraud any director, key managerial personnel, other officer of the company or any other person or entity, has taken undue advantage or benefit, whether in the form of any asset, property or cash or in any other manner, **the Central Government may file an application before the Tribunal for appropriate orders** with

regard to **disgorgement of such asset, property, or cash**, as the case may be, and also for holding such director, key managerial personnel, officer or other person liable personally without any limitation of liability. (Refer example given in section 212)



19. EXPENSES OF INVESTIGATION (SECTION 225 OF THE COMPANIES ACT, 2013)

Section 225 of the Companies Act, 2013 lays down the following provisions in respect of expenses of investigation:

- (i) **Reimbursement of expenses:** The expenses of, and incidental to, an investigation by an inspector appointed by the Central Government under this Chapter (Chapter XIV- Inspection, Inquiry and Investigation) other than expenses of inspection under section 214 (Security for payment of costs and expenses of investigation) shall be defrayed in the first instance by the Central Government, but **shall be reimbursed by the following persons** to the extent mentioned below, namely:—

any person who is convicted on a prosecution instituted, or

who is ordered to pay damages , or

restore any property in proceedings brought

Extent of reimbursement: Reimbursement to the extent that he may in the same proceedings be ordered to pay the said expenses as may be specified by the court convicting such person, or ordering him to pay such damages or restore such property, as the case may be;

Any company or body corporate in whose name proceedings are brought, to the extent of the amount or value of any sums or property recovered by it as a result of such proceedings;

Where a prosecution is instituted: unless, as a result of the investigation, a prosecution is instituted under section 224,—

- (1) any company, body corporate, managing director or manager dealt with by the report of the inspector; and
- (2) the applicants for the investigation, where the inspector was appointed under section 213,

to such extent as the Central Government may direct.

- (ii) **Extent of liability:** Any amount for which a company or body corporate is liable, shall be a **first charge** on the sums or property mentioned in that clause.



20. VOLUNTARY WINDING UP OF COMPANY, ETC., NOT TO STOP INVESTIGATION PROCEEDINGS (SECTION 226 OF THE COMPANIES ACT, 2013)

Section 226 of the Companies Act, 2013 provides that an investigation under this Chapter may be initiated notwithstanding, and no such investigation shall be stopped or suspended by reason only of, the fact that—

- (a) an **application** has been made **under section 241** (Application to Tribunal for relief in cases of oppression, etc.);
- (b) **the company** has passed a **special resolution for voluntary winding up**; or
- (c) any **other proceeding for the winding up** of the company is **pending** before the Tribunal.

Where a winding up order is passed by the Tribunal in a proceeding referred to in clause (c), the inspector shall inform the Tribunal about the pendency of the investigation proceedings before him and the Tribunal shall pass such order as it may deem fit.

Nothing in the winding up order shall absolve any director or other employee of the company from participating in the proceedings before the inspector or any liability as a result of the finding by the inspector.



21. LEGAL ADVISERS AND BANKERS NOT TO DISCLOSE CERTAIN INFORMATION (SECTION 227 OF THE COMPANIES ACT, 2013)

Section 227 of the Companies Act, 2013 provides for non-disclosure of certain information by certain persons.

Nothing in this Chapter shall require the disclosure to the Tribunal or to the Central Government or to the Registrar or to an inspector appointed by the Central Government—

- (a) **by a legal adviser**, of any privileged communication made to him in that capacity, except as respects the name and address of his client; or
- (b) **by the bankers** of any company, body corporate, or other person, of any information as to the affairs of any of their customers, other than such company, body corporate, or person.



22. INVESTIGATION ETC. OF FOREIGN COMPANIES (SECTION 228 OF THE COMPANIES ACT, 2013)

Section 228 of the Companies Act, 2013 provides for Investigation etc. of foreign companies. According to this section:

The provisions of this Chapter (Chapter XIV- Inspection, Inquiry and Investigation) shall apply *mutatis mutandis* to inspection, inquiry or investigation in relation to foreign companies.



23. PENALTY FOR FURNISHING FALSE STATEMENT, MUTILATION, DESTRUCTION OF DOCUMENTS (SECTION 229 OF THE COMPANIES ACT, 2013)

Section 229 of the Companies Act, 2013 lays down the following penalty for furnishing false statement, mutilation, destruction of documents:

Where **a person** who is required to provide an explanation or make a statement during the course of inspection, inquiry or investigation, or **an officer or other employee** of a company or other body corporate which is also under investigation, shall be punishable for fraud in the manner as provided in section 447, if he—

- (a) destroys, mutilates or falsifies, or or conceals tampers or unauthorizedly removes, or is a party to the **destruction, mutilation or falsification or concealment or tampering or unauthorized removal** of, documents relating to the property, assets or affairs of the company or the body corporate;
- (b) makes, or is a party to the making of, **a false entry in any document** concerning the company or body corporate; or
- (c) provides an **explanation which is false** or which he knows to be false,

TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. *At an Extra-ordinary General Meeting of Ravi Share-brokers Limited, held at its Registered Office situated at Rajendra Place, New Delhi, the shareholders passed a special resolution to the effect that the affairs of the company ought to be investigated. Ravi Share-brokers Limited, thereafter, submitted the special resolution so passed to the Central Government for further action. Under the given situation, you are required to select the appropriate option from those given below:*
 - (a) *Power of the Central Government to order an investigation into the affairs of Ravi Share-brokers Limited as requested in the special resolution so submitted by the company is discretionary and therefore, it may or may not order an investigation.*
 - (b) *Power of the Central Government to order an investigation into the affairs of Ravi Share-brokers Limited as requested in the special resolution so submitted by the company is mandatory and therefore, it shall order an investigation.*
 - (c) *Central Government is not empowered to pass order of investigation in case of non-government companies and therefore, no order of investigation into the affairs of Ravi Share-brokers Limited as requested in the special resolution so submitted by the company shall be ordered.*
 - (d) *Power of the Central Government to order an investigation into the affairs of Ravi Share-brokers Limited can be initiated just on request by the company.*

2. *Sanchita Tech Mart Limited is in the grip of serious apprehensions that its shares might be cornered by a group of unscrupulous persons and if it happens, it would certainly result in change in the Board of Directors which might be prejudicial to the public interest. With a view to impose restrictions, Ramneek, one of the directors of Sanchita TechMart Limited, seeks your advice as to how the company can impose restrictions on the transfer of shares of the company. Choose the correct option from those given below:*
 - (a) *Sanchita Tech Mart Limited can make an application to the National Company Law Tribunal (NCLT) under Section 222 for imposition of restrictions on securities.*
 - (b) *Sanchita Tech Mart Limited can make an application to the Central Government under Section 222 for imposition of restrictions on securities.*
 - (c) *Sanchita Tech Mart Limited can make an application to the National Company Law Tribunal (NCLT) under Section 216 for investigation into the ownership of company.*

- (d) Sanchita Tech Mart Limited can make an application to the Central Government under Section 216 for investigation into the ownership of the company.
3. After perusal of the inspector's report made under Section 223 of the Companies Act, 2013, it appears to the Central Government that some action is required to be taken against a company, it may cause to be presented to the Tribunal:
- (a) A petition for the winding up of the company on the ground that it is just and equitable that it should be wound up.
- (b) An application under Section 241 of the Companies Act, 2013.
- (c) Both (a) and (b)
- (d) A petition for the merger of the company on the ground that it is just and equitable that it should be merged.
4. Under the garb of cement business, some of the directors of Royal Cement Limited, a company incorporated in the year 2001 and having its factories at Rohtak and Bhiwani, were involved in several illegal activities. In such a situation, on receipt of a report of the Registrar of Companies or inspector under Section 208 or in the public interest or on request from any Department of the Central Government or a State Government, the Central Government may, by order, assign the investigation into the affairs of Royal Cement Limited to the Serious Fraud Investigation Office (SFIO). In addition to the above bases, there is one more basis which may prompt the Central Government to assign the investigation to the Serious Fraud Investigation Office (SFIO). From the following four options, choose such appropriate basis for assigning the investigation to the SFIO.
- (a) On intimation through an Ordinary Resolution passed by the shareholders of Royal Cement Limited that the affairs of the company are required to be investigated.
- (b) On intimation through a Special Resolution passed by the shareholders of Royal Cement Limited that the affairs of the company are required to be investigated.
- (c) On an intimation received from certain senior employees of Royal Cement Limited that the affairs of the company are required to be investigated.
- (d) On an intimation received from certain ex-directors of Royal Cement Limited that the affairs of the company are required to be investigated.
5. Mr. Raman, an Inspector appointed under Section 212 of the Companies Act, 2013, started investigations into the affairs of C-Tech Innovative Solutions Ltd. During the process of investigation, Mr. Raman noticed certain unusual facts and information regarding the transactions made by C-Tech Innovative Solutions Ltd. with its subsidiary company Shyamala InfoTech Solutions Ltd. Based on the information so collected from the investigation, Mr. Raman wanted to investigate the affairs of Shyamala InfoTech Solutions Ltd. also. Out of the

following options, which one correctly indicates whether Mr. Raman can proceed with the investigation of the affairs of subsidiary company Shyamala InfoTech Solutions Ltd. or not in the light of the applicable provisions of the Companies Act, 2013.

- (a) Mr. Raman shall be able to proceed with the investigation of the affairs of subsidiary company Shyamala InfoTech Solutions Ltd. after obtaining the prior approval of the Director, Serious Fraud Investigation Office (SFIO).
 - (b) Mr. Raman shall not be able to proceed with the investigation of the affairs of subsidiary company Shyamala InfoTech Solutions Ltd. since it is not within his powers to undertake investigation of any other entity.
 - (c) Mr. Raman shall be able to proceed with the investigation of the affairs of subsidiary company Shyamala InfoTech Solutions Ltd. after obtaining the prior approval of the National Company Law Tribunal in whose jurisdiction the registered office of the subsidiary company is located.
 - (d) Mr. Raman shall be able to proceed with the investigation of the affairs of subsidiary company Shyamala InfoTech Solutions Ltd. after obtaining the prior approval of the Central Government.
6. Sunder Cosmetics Limited was served a notice by the jurisdictional Registrar of Companies to produce at his office for inspection of certain more books of accounts, other books, papers and explanations, etc. at 11 A.M. on January 5, 2022. Choose the applicable option from those given below that indicates the reason for such inspection by the concerned Registrar of Companies:
- (a) Since no information or explanation was furnished by Sunder Cosmetics Limited to the Registrar of Companies within the time specified in the earlier notice issued by him.
 - (b) Since Registrar of Companies, on an examination of the documents furnished by Sunder Cosmetics Limited, was of the opinion that the information or explanation furnished by the company was inadequate.
 - (c) Since Registrar of Companies was satisfied on a scrutiny of the documents furnished by Sunder Cosmetics Limited, that an unsatisfactory state of affairs existed in the company and the information or documents so furnished did not disclose a full and fair statement of the information required.
 - (d) In all of the situations given above in option (a), (b) and (c), inspection can be preferred.

Descriptive Questions

1. Provide various grounds on which the investigation is assigned to Serious Fraud Investigation Office?
2. Discuss the powers of Inspectors regarding investigation into affairs of related companies.
3. A group of creditors of XYZ Limited makes a complaint to the Registrar of Companies, Gujarat alleging that the management of the company is indulging in destruction and falsification of the accounting records of the company. The complainants request the Registrar to take immediate steps to seize the records of the company so that the management may not be allowed to tamper with the records. The complaint was received at 11 A.M. on 06th June, 2018 and the registrar has attempted to enter the premise of company but has been denied by the company, due to not having order from special court.

Is the contention of company being valid in terms of Companies Act, 2013?

4. Mr. Atul is an employee of the company ABC Limited and investigation is going on him under the provisions of Companies Act, 2013. The company wants to terminate the employee on the ground of investigation is going against him. They have filed the application to tribunal for approval of termination. Company has not received any reply from the tribunal within 30 days of filing an application. The company consider it as a deemed approval and terminated Mr. Atul.
 - (a) *Is the contention of company being valid in law?*
 - (b) *What is remedy available to Mr. Atul?*
 - (c) *What is remedy available to Mr. Atul, if reply of Tribunal has been received within 30 days of application?*
5. A group of shareholders of FMG Limited made a complaint to the concerned Registrar of Companies (RoC) that the business of the Company is being carried on for unlawful and fraudulent purposes and filed an application to enquire into the affairs of the Company. Referring to and analyzing the provisions of the Companies Act, 2013, decide:
 - (i) *Whether the RoC has the power to order for an inquiry into the affairs of the Company?*
 - (ii) *If yes, state the procedure to be followed by the RoC.*
 - (iii) *Whether the inquiry should be pursued by the RoC in case the complaint is withdrawn by the same group of shareholders subsequent to the Order for enquiry?*
 - (iv) *Whether the Central Government has the power to direct the RoC to carry out the inquiry?*

ANSWERS

Answer to Multiple Choice Questions

1.	a	2.	a	3.	c	4.	b	5.	d
6.	d								

Answer to Descriptive Questions

- As per section 212 of the Companies Act, 2013, the Central Government may assign the investigation into affairs of a company to the Serious Frauds Investigation Office on the basis of an opinion formed from the following:
 - After the inspection of books of account or papers or inquiry the Registrar shall submit a written report to the Central Government. The report may recommend the need for further investigation along with reasons in support. The Central Government on receipt of such report can order an investigation under Serious Frauds Investigation Office.
 - The company may pass a special resolution and can request Central Government to investigate into the affairs of the company.
 - The Central Government can order investigation under Serious Frauds Investigation Office, in public interest.
 - The departments Central Government and State Governments can request for investigation under Serious Frauds Investigation Office.
- Section 219 states that**, if the inspector appointed under Sections 210, 212 or 213 to investigate into the affairs company considers it necessary for the purposes of the investigation to investigate, he can do the investigation of the affairs of other related companies or body corporate with the prior approval of the Central Government.
 - Holding or Subsidiary Company:** which is or has been at the relevant time been the company's subsidiary or holding or subsidiary of its holding company;
 - Related Party:** which is or has been at the relevant time been managed by any person as a managing director or manager who is or was at the relevant time the managing director or the manager of the company;
 - Deemed Control:** whose Board of Directors' comprises nominees of the company or is accustomed to act in accordance with the directions of the company or any of its directors; or
 - In Employment of Company:** in case any person is or has at any relevant time been the company's managing director or manager or employee.

The results of the investigation are relevant to the investigation of the affairs of the company for which he is appointed.

3. Section 209, of the Companies Act, 2013 states that, if the Registrar has **reasonable ground to believe** that the books and papers of

- A company or
- relating to the key managerial personnel or
- any director or
- auditor or
- company secretary in practice if the company has not appointed a company secretary are likely to be destroyed, mutilated, altered, falsified or secreted he may, after obtaining an order from the special court for the seizure of such books and papers,
 - (a) enter with such assistance as may be required and search the place where such books or papers are kept; and
 - (b) seize such books and papers as he considers necessary after allowing the company to take copies or extracts there from.

According to the above provisions the registrar may enter, search and seize the books only after obtaining an order from the Special Court.

In the given scenario, the registrar has failed to obtain permission from the special court so, he is not authorized to enter the premises of the company and seize the books of accounts of XYZ Limited. Hence, the contention of the XYZ Limited is valid in law.

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

The company shall require approval in the following circumstances:

- discharge or suspension of an employee; or
- punishment to an employee by dismissal, removal, reduction in rank or otherwise; or
- change in the terms of employment to the disadvantage of employee(s);

The Tribunal shall notify its objection to the action proposed in writing.

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

Appeal to the Appellate Tribunal

If the company, other body corporate or person concerned is dissatisfied with the objection raised by the Tribunal, it may, within a period of 30 days of the receipt of the notice of the objection, refer an appeal to the Appellate Tribunal in such manner and on payment of fees of INR 1,000 as per the schedule of Fees.

The decision of the Appellate Tribunal on such appeal shall be final and binding on the Tribunal and on the company, other body corporate or person concerned.

- (a) Yes, the termination of Mr. Atul made by the company is totally valid in law and company can do so by considering deemed approval of tribunal.
 - (b) In this scenario, Mr. Atul has not any remedy available. As per the provision of the law appeal to the appellate tribunal can be made only if the person is dissatisfied with the objection raised by the tribunal. Hence, in this case the tribunal has not replied Mr. Atul cannot refer an appeal to Appellate Tribunal.
 - (c) In this case, Mr. Atul can refer and appeal to appellate tribunal within 30 days of the receiving letter of objection raised by the tribunal and with payment of Fees of Rs. 1,000 as per schedule of Fees.
- 5.
- (i) Yes, the RoC has the power to order for an inquiry as he deems fit after providing the company a reasonable opportunity of being heard, into the affairs of the company if he is satisfied on a representation made to him by any person that the business of a company is being carried on for a fraudulent or unlawful purpose or not in compliance with the provisions of this Act. [Section 206(4) of the Companies Act, 2013]
 - (ii) Procedure followed by RoC: The Registrar may, after informing the company of the allegations made against it by a written order, call on the company to furnish in writing any information or explanation on matters specified in the order within such time as he may specify therein and carry out such inquiry as he deems fit after providing the company a reasonable opportunity of being heard.
 - (iii) The inquiry can be pursued by the ROC in case the complaint is withdrawn by same group of shareholders subsequent to the order for inquiry in terms of section 206(4).
 - (iv) Yes, the Central Government may, if it is satisfied that the circumstances so warrant, direct the Registrar for the purpose to carry out the inquiry under section 206(4).

[illegible]

CHAPTER

5

COMPROMISES, ARRANGEMENTS AND AMALGAMATIONS



LEARNING OUTCOMES

By the end of this Chapter, you will be able to:

- ❑ Explain the concepts of Compromise, Arrangement, Merger and Amalgamation
- ❑ Describe the powers of Company, Members, Central Government or Tribunal in respect of Compromise or Arrangements with members or creditors
- ❑ Explain Fast Track Mergers and Cross Border Mergers
- ❑ Elaborate Power of Central Government to order Mergers and Amalgamation in the public interest
- ❑ Explain as to how to acquire shares of shareholders dissenting from scheme or contract approved by majority
- ❑ Describe the provisions related to purchase of minority shareholding



1. INTRODUCTION

Mergers and acquisitions have always been a topic of corporate interest in the modern times. The complexity of the laws governing these modes of corporate restructuring makes them even more intriguing and mystifying.

Important terms:

'**Compromise**' means a **peaceful or willing settlement of a dispute** by mutual adjustments and concessions. Thus, in 'compromise' each party has to yield and give some concessions. Compromise assumes a dispute.

In '**arrangement**' there is no dispute, but **it modifies rights**. Such readjustment of rights may be with members or class of them or creditors or a class of them. The term 'arrangement' is very wide and can include a reorganization of capital.

The 'arrangement' or 'compromise' may be with the creditors or the members.

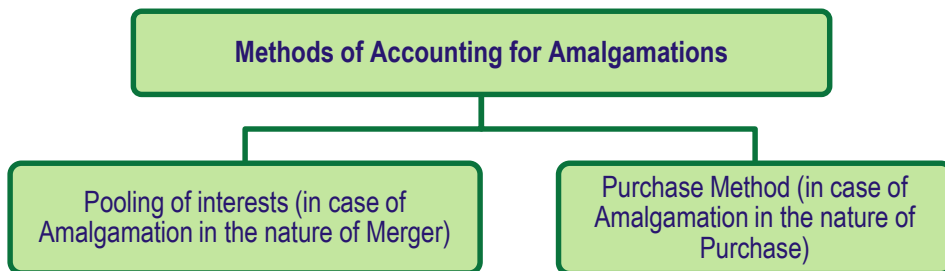
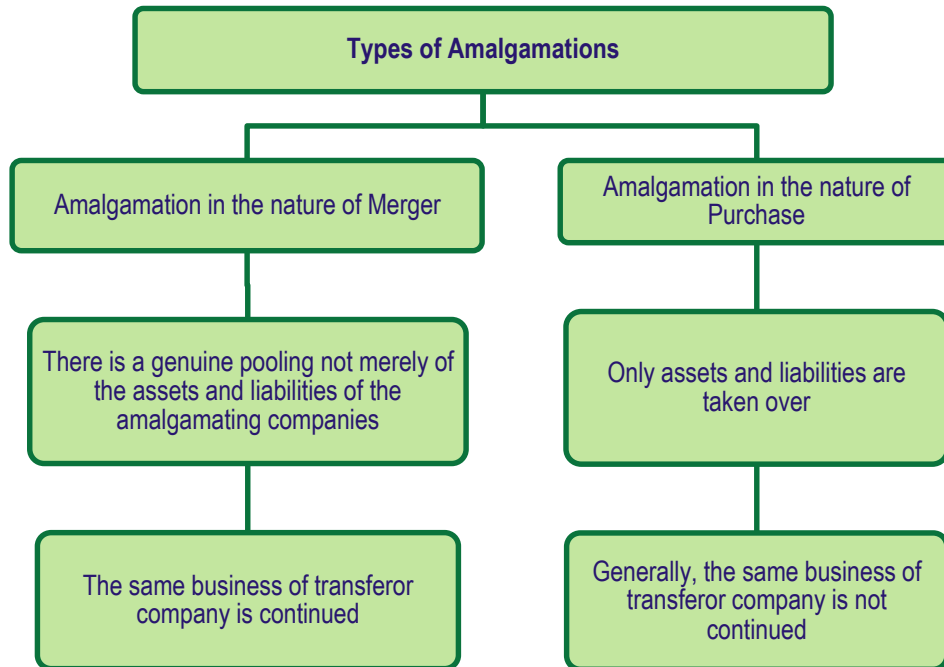
For **example** - Arrangement and compromise are as creditors agreeing to waive part of their dues; converting part or all dues of creditors into shares; extending time for payment; reduction in share capital by members; amalgamation; full or part transfer of undertaking, property or liabilities of the company to another company, etc.

Amalgamation

- Amalgamation means an amalgamation pursuant to the provisions of the Companies Act, 2013 or any other statute which may be applicable to companies and includes 'merger'.
- Transferor Company means the company which is amalgamated into another company.
- Transferee Company means the company into which a transferor company is amalgamated.
- Merger, reconstruction and amalgamation are the schemes of compromise and arrangement.

Reconstruction

- It is usually of only one company while amalgamation involves two or more companies.
- 'Reconstruction' literally means 'building again'. It implies reorganization with alteration or modification of rights of members or creditors or both.
- Existing business is carried out in some altered form.
- Reconstruction usually involves reduction in value of shares, making fully paid up shares as partly paid so that further amounts can be called, transfer of undertaking to another company, take-over by another company, satisfaction of rights of shareholders by allotting them shares in new company etc.

Types of Amalgamations

Thus, amalgamation is blending of two or more existing undertakings into one undertaking. The shareholders of each blending company become substantially the shareholders in the company which is to carry on the blending undertakings. There may be amalgamation either by the transfer of two or more undertakings to a new company, or by the transfer of one or more undertakings to an existing company.

Now we will see the two types of amalgamations in detail -

Amalgamation in the Nature of Merger

Amalgamation in the nature of merger is an amalgamation which satisfies **all the following conditions** -

- (i) **All the assets and liabilities** of the transferor company become, after amalgamation, the assets and liabilities of the transferee company.
- (ii) Shareholders holding not less than **90% of the face value of the equity shares** of the transferor company (other than the equity shares already held therein, immediately before the amalgamation, by the transferee company or its subsidiaries or their nominees) **shall become equity shareholders of the transferee company** by virtue of the amalgamation.
- (iii) The **consideration** for the amalgamation **receivable** by those equity shareholders of the transferor company who agree to become equity shareholders of the transferee company is discharged by the transferee company **wholly by the issue of equity shares in the transferee company**, except that cash may be paid in respect of any fractional shares.
- (iv) The **business of the transferor company is intended to be carried on**, after the amalgamation, by the transferee company.
- (v) **No adjustment** is intended to be **made to the book values of the assets and liabilities of the transferor company** when they are incorporated in the financial statements of the transferee company except to ensure uniformity of accounting policies.

Amalgamation in the Nature of Purchase

Amalgamation in the nature of purchase is an amalgamation which **does not satisfy any one or more of the conditions** specified above.

Chapter XV covering Section **230 to 240** of Companies Act, 2013 contains the provisions relating to the Compromises, Arrangements and Amalgamations.

The compromise, arrangement, amalgamation and reconstruction **require the approval of National Company Law Tribunal (NCLT)**. Chapter XV is a complete code in itself which contains provisions regarding all forms of compromises with creditors and arrangements with members. The procedural aspects involved such as format of application to be made to National Company Law Tribunal (NCLT), form of notice and the procedural aspects involved with respect to the substantive law are covered under the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 made under Chapter XV of the Companies Act, 2013.

Important aspects of this Chapter are as follows:

- (i) This chapter provides the provisions which specify the **detailed disclosures to be made during the process of corporate restructuring**. This requirement of extensive disclosures is to ensure transparency and allows stakeholders to take decisions.
- (ii) Introduction of **voting by way of postal ballot** will ensure larger public participation.
- (iii) Introduction of **concept of dispensation** by providing a threshold for the dispensation of creditors' meetings.

- (iv) This chapter also requires **serving of notices to the various statutory authorities** with regard to the scheme, arrangement or restructuring, so that participation of various regulators may assist the Tribunal to take an informed decision.
- (v) Provisions relating to **takeover of listed companies** through the scheme of compromise or arrangement, emphasis on the pricing guidelines which the Securities and Exchange Board of India (SEBI) would prescribe ensuring uniformity in law.
- (vi) This chapter also contains provisions which **prohibit the maintenance of treasury stock**. The practice of indirectly holding investments through intermediaries is now prohibited and cannot be structured by companies.
- (vii) **Exit options to shareholders** through pre-determined formula or valuation can be given on merger of listed company with an unlisted company.
- (viii) Statement **certifying** implementation of the scheme shall be given by a Chartered Accountant or a Company Secretary.
- (ix) The provisions contained in this chapter are in consonance with the SEBI regulations and guidelines issued by RBI.
- (x) This chapter provides for **Fast Track amalgamations** between-
 - Two or more small companies, or
 - Holding company and its wholly owned subsidiaries.
- (xi) Enables **cross border amalgamations** between Indian Companies and Foreign Companies.
- (xii) Lays the mechanism under which the transferee company under a scheme or contract can acquire **shares of dissenting shareholders**.
- (xiii) Provides **exit method for minority shareholders**, and promoters to have 100% promoter entity so that balance between the interests of the promoters and minority shareholders may be maintained.
- (xiv) This chapter also provides the process of **amalgamation of companies in public interest**.
- (xv) **Books and Papers** of the amalgamated company/ the company whose shares have been acquired by another company shall **not be disposed** of without prior permission of the Central Government.
- (xvi) **Liability of the officers** of the transferor company on any offence committed under this Act shall be **retrospective** even after the merger, amalgamation or acquisition.



2. POWER TO COMPROMISE OR MAKE ARRANGEMENTS WITH CREDITORS AND MEMBERS [SECTION 230]

Power to Compromise or Make Arrangements with Creditors and Members [Section 230]

Sub-Sec. (1)	• Power of Tribunal to call for a meeting on an application filed for a compromise or arrangement
Sub-Sec. (2)	• Disclosures by Applicant
Sub-Sec. (3)	• Notice of meeting to be conducted on order of Tribunal
Sub-Sec. (4)	• Vote to the adoption of Compromise or Arrangement
Sub-Sec. (5)	• Notices to sectoral regulators to make representation, if likely to be affected by the compromise or arrangement
Sub-Sec. (6)	• Binding order of Tribunal
Sub-Sec. (7)	• Particulars to be stated in the order of Tribunal
Sub-Sec. (8)	• Filing of Order of Tribunal with Registrar
Sub-Sec. (9)	• The Tribunal may dispense with calling of a meeting
Sub-Sec. (10)	• Exemption in relation to Buy-back of Securities
Sub-Sec. (11)	• Inclusion of Takeover Offer
Sub-Sec. (12)	• Application to Tribunal by Aggrieved Party

Section 230 of Companies Act, 2013 deals with the basic procedures to be followed in respect of any compromise or arrangement, calling of meetings of creditors, members and other security-holders for approval of the scheme and other allied matters. It also describes powers of NCLT. The provisions of Section 230 are given below:

(1) **Power of Tribunal to call for a meeting on an application filed for a compromise or arrangement [Sub-section 1]:**

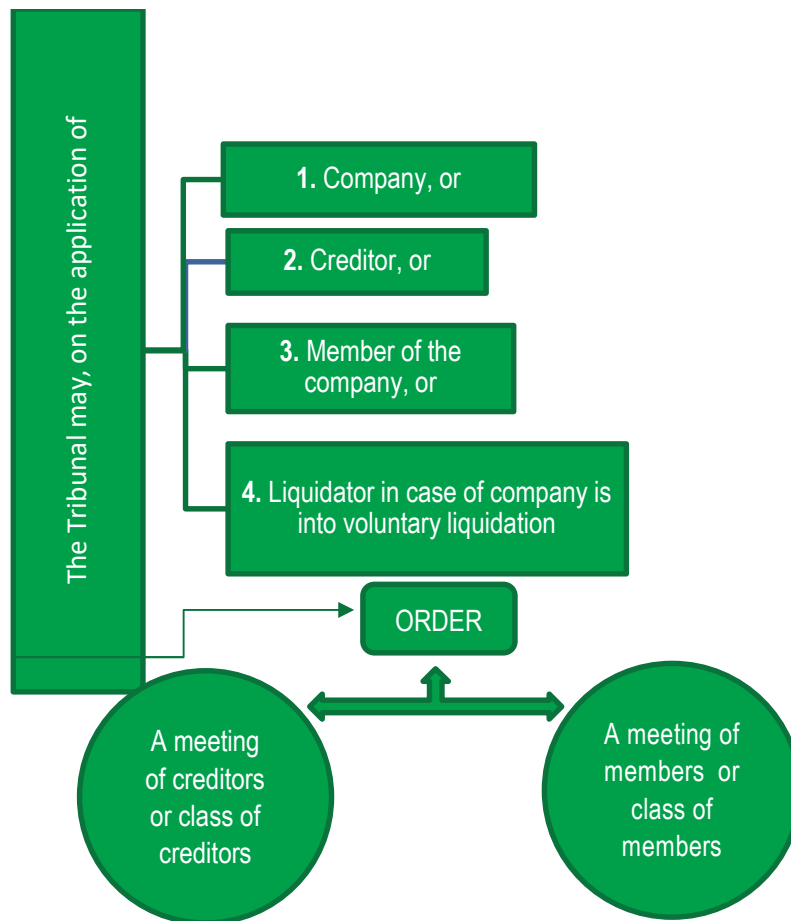
Where a compromise or arrangement is proposed between—

- (a) **a company and its creditors** or any class of them; or

(b) a company and its members or any class of them,
the Tribunal may, on the application of the-

- Company; or
- Creditor; or
- Member of the Company; or
- Liquidator (in case the company is going for voluntary liquidation)

order a meeting of the creditors or class of creditors, or of the members or class of members, as the case may be, to be **called, held and conducted** in such manner as the Tribunal directs.



Explanation— For the purposes of this sub-section, **arrangement** includes a reorganization of the company's share capital by the consolidation of shares of different classes or by the division of shares into shares of different classes, or by both of those methods.

(2) **Disclosures by person who makes an application for compromise or arrangement [Sub-section (2)]:**

The Company or any other person, by whom an application is made, shall disclose to the Tribunal by affidavit—

- (a) **all material facts** relating to the company, such as the latest financial position of the company, the latest auditor's report on the accounts of the company and the pendency of any investigation or proceedings against the company;
- (b) **reduction of share capital** of the company, if any, included in the compromise or arrangement;
- (c) **any scheme of corporate debt restructuring** consented to by **not less than seventy-five percent of the secured creditors in value**, including—
 - (i) a creditor's responsibility statement in the prescribed form;
 - (ii) safeguards for the protection of other secured and unsecured creditors;
 - (iii) report by the auditor that the fund requirements of the company after the corporate debt restructuring as approved shall conform to the liquidity test based upon the estimates provided to them by the Board;
 - (iv) where the company proposes to adopt the corporate debt restructuring guidelines specified by the Reserve Bank of India, a statement to that effect; and
 - (v) a valuation report in respect of the shares and the property and all assets, tangible and intangible, movable and immovable, of the company by a registered valuer.

(3) **Notice of meeting to be conducted on order of Tribunal [Sub-section (3)]:**

Where a meeting is proposed to be called in pursuance of an order of the Tribunal, a notice of such meeting shall be sent to:

- all the creditors or class of creditors;
- all the members or class of members; and
- the debenture-holders of the company,

individually at the address registered with the company.

Note: As per Section 230 (5), the notice of the meeting shall also be sent to the sectoral regulators and the authorities which are likely to be affected by the compromise or arrangement. This is explained later in the chapter.

The notice of the meeting to be conducted on the Order of Tribunal shall be sent to:

-  to all the creditors or class of creditors individually at the address registered with the company;
-  to all the members or class of members individually at the address registered with the company;
-  to the debenture-holders of the company individually at the address registered with the company;
-  Sectoral regulators and other authorities mentioned in section 230 (5).

Annexure with Notice: Notice of meeting shall be accompanied by a statement disclosing the following:

Annexure with Notice	details of the compromise or arrangement,
	a copy of the valuation report, if any, and
	explaining their effect on creditors, key managerial personnel, promoters and non-promoter members, and the debenture-holders and
	the effect of the compromise or arrangement on any material interests of the directors of the company or the debenture trustees, and
	such other matters as may be as prescribed under Rule 6 of the Companies (Compromises, arrangements and amalgamations) Rules, 2016.

Advertisement of notice: Such notice and other documents shall also be placed on -

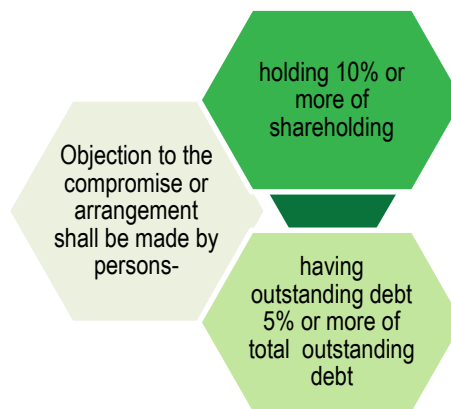
- the website of the company, if any, and
- in case of a listed company, these documents shall be sent to the Securities and Exchange Board of India (SEBI) and stock exchange where the securities of the companies are listed, for placing on their website and
- shall also be published in newspapers in the manner prescribed under Rule 7 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016.

Time period for the receipt of the copies of the compromise or arrangement: Where the notice for the meeting is also issued by way of an advertisement, it shall indicate the time within which copies of the compromise or arrangement shall be made available to the concerned persons free of charge from the registered office of the company.

(4) **Vote to the adoption of the compromise or arrangement [Sub-section (4)]:**

A notice shall provide that the persons **to whom the notice is sent may vote** in the meeting either themselves or through proxies or by postal ballot to the adoption of the compromise or arrangement within **one month** from the date of receipt of such notice:

Provided that any objection to the compromise or arrangement shall be made only by persons holding not less than ten per cent of the shareholding or having outstanding debt amounting to not less than five per cent of the total outstanding debt as per the latest audited financial statement.

(5) **Notices to sectoral regulators to make representation, if likely to be affected by the compromise or arrangement [Sub-section (5)]:**

A notice along with all the documents in such form as may be prescribed shall also be sent to-

- the Central Government,
- the income-tax authorities,
- the Reserve Bank of India,
- the Securities and Exchange Board,
- the Registrar,
- the respective stock exchanges,
- the Official Liquidator,
- the Competition Commission of India established under the Competition Act, 2002, if necessary,
- and such other sectoral regulators or authorities which are likely to be affected by the compromise or arrangement and

shall require that **representations**, if any, to be made by them shall be made within a period of **thirty days** from the date of receipt of such notice, failing which, it shall be presumed that they have no representations to make on the proposals.

(6) **Binding order of Tribunal [Sub-section (6)]:**

Where, at a meeting held, majority of persons representing **three-fourths in value** of the creditors, or class of creditors or members or class of members, as the case may be, voting in person or by proxy or by postal ballot, **agree to any compromise or arrangement** and if such compromise or arrangement is **sanctioned by the Tribunal** by an order, the same **shall be binding** on the company, all the creditors, or class of creditors or members or class of members, as the case may be, or, in case of a company being wound up, on the liquidator, "appointed under the Companies Act, 2013 or under the Insolvency and Bankruptcy Code, 2016, as the case may be," and the contributories of the company.

(7) **Particulars to be stated in the order [Sub-section (7)]:**

An order made by the Tribunal, shall provide for all or any of the following matters, namely:—

- (a) **where the compromise or arrangement provides for conversion of preference shares into equity shares**, such preference shareholders shall be given an option to either obtain arrears of dividend in cash or accept equity shares equal to the value of the dividend payable;
- (b) the **protection of any class** of creditors;
- (c) if the compromise or arrangement results in the **variation of the shareholders' rights**, it shall be given effect to under the provisions of section 48;
- (d) if **the compromise or arrangement is agreed to by the creditors** under sub-section (6), any proceedings pending before the Board for Industrial and Financial Reconstruction (BIFR) established under section 4 of the Sick Industrial Companies (Special Provisions) Act, 1985 shall abate;
- (e) **such other matters** including exit offer to dissenting shareholders, if any, as are in the opinion of the Tribunal necessary to effectively implement the terms of the compromise or arrangement:

Provided that no compromise or arrangement shall be sanctioned by the Tribunal unless a certificate by the company's auditor has been filed with the Tribunal to the effect that the accounting treatment, if any, proposed in the scheme of compromise or arrangement is in conformity with the accounting standards prescribed under section 133.

(8) **Filing of order of tribunal with registrar [Sub-section (8)]:**

The order of the Tribunal shall be filed with the Registrar by the company **within** a period of **thirty days** of the receipt of the order.

- (9) **The Tribunal may dispense with calling of a meeting** of creditor or class of creditors where such creditors or class of creditors, having at least ninety per cent value, agree and confirm, by way of affidavit, to the scheme of compromise or arrangement. **[Sub-section (9)]**

- (10) **Compromise in relation to buy-back of securities [sub-section (10)]:**

No compromise or arrangement in respect of any buy-back of securities under this section shall be sanctioned by the Tribunal unless such buy-back is in accordance with the provisions of section 68.

- (11) **Inclusion of takeover offer [Sub-section (11)]:**

Any compromise or arrangement may include **takeover offer** made in such manner as may be prescribed.

Provided that in case of listed companies, takeover offer shall be as per the regulations framed by the Securities and Exchange Board of India (SEBI).

- (12) **Application to Tribunal by aggrieved party [Sub-section (12)]:**

An aggrieved party may make an **application to the Tribunal** in the event of any grievances with respect to the **takeover offer of companies other than listed companies** in such manner as may be prescribed and the Tribunal may, on application, pass such order as it may deem fit.

Explanation— For the removal of doubts, it is hereby declared that the provisions of section 66 (reduction of share capital) shall not apply to the reduction of share capital effected in pursuance of the order of the Tribunal under this section.

Since reduction of share capital requires an application to Tribunal by company after passing Special Resolution and on confirmation by Tribunal, reduction of share capital gets effected. However, in the case of compromise under section 230 if that results into reduction of capital, compliance of section 66 is not required to be made separately in such cases.

Example 1: Icon Stars Limited applied to the Tribunal for a scheme of arrangement between the company and its members under section 230 of the Companies Act, 2013. Accordingly, a meeting was ordered by the Tribunal to be conducted between the company and its members for considering the scheme of arrangement. Some of the members of the company to whom notices were sent had raised certain objections to the scheme of arrangement.

As per the proviso to the provisions section 230 (4) of the Companies Act, 2013, any objection to the compromise or arrangement shall be made only by persons holding **not less than ten percent** of the shareholding or having outstanding debt amounting to not less than five percent of the total outstanding debt as per latest audited financial statements.

1. Supreme Court in *Joint Commissioner of Income-tax (OSD) v. Reliance Jio Infocomm Ltd.*, September 9, 2022 laid that where IT department opposed composite scheme of arrangement of petitioner companies on ground that scheme was a tool to avoid and evade taxes, NCLT as well as

NCLAT having clarified that IT department was entitled to take out appropriate proceedings for recovery of any tax statutorily due from transferor or transferee company or any other person who was liable for payment of such tax due, impugned judgment and orders passed by NCLAT as well as NCLT approving scheme could not have been interfered with.

As per the fact, a composite scheme of arrangement between petitioner companies was approved by NCLT. Income tax department opposed said scheme on ground that conversion of preference shares into loan would substantially reduce profitability of demerged company, which would act as a tool to avoid and evade taxes. NCLAT by impugned order held that without going to record and without placing any evidence to substantiate allegation by appearing before Tribunal, it was not open to Income-tax department to hold that overall scheme of arrangement was giving undue favour to shareholders of company and resulted into tax avoidance and approval by NCLT to such scheme was not to be interfered with. On appeal before Supreme Court, Joint Commissioner of Income-tax submitted that impugned orders and/or sanction of Scheme might come in way of Department while framing assessment and to that extent, interest of revenue would be affected. However, NCLT as well as NCLAT had already clarified that IT department would be entitled to take out appropriate proceedings for recovery of any tax statutorily due from transferor or transferee company or any other person who was liable for payment of such tax due. Held, therefore, that impugned judgment and orders passed by NCLAT as well as NCLT approving scheme could not have been interfered with.

2. National Company Law Appellate Tribunal, New Delhi, in *Ramesh Kumar Chaudhary v. Anju Agarwal, Liquidator of Shree Bhawani Paper Mills Ltd.*, March 15, 2022, laid down that Scheme for Compromise or Arrangement submitted under section 230 ought to have consent of not less than 75 per cent of secured creditors, and an affidavit to that effect ought to accompany with Scheme and obligation to obtain consent of 75 per cent of creditors is on person who proposes Scheme; where no opportunity was provided to proposers to explain and clarify their scheme, they were to be allowed time to submit revised scheme.



3. POWER OF TRIBUNAL TO ENFORCE COMPROMISE OR ARRANGEMENT [SECTION 231]

The provisions of section 231 of the Companies Act, 2013 are detailed below:

- (1) **Power of Tribunal to implement the order:** Where the Tribunal makes an order under section 230 sanctioning a compromise or an arrangement in respect of a company, it—
 - (a) shall have **power to supervise the implementation** of the compromise or arrangement; and
 - (b) may, at the time of making such order or at any time thereafter, **give such directions** in regard to any matter or make such modifications in the compromise or arrangement as it may consider necessary for the **proper implementation** of the compromise or arrangement.

- (2) **Passing of Winding up order by Tribunal:** If the Tribunal is satisfied that the compromise or arrangement sanctioned under **section 230 cannot be implemented satisfactorily with or without modifications**, and the company is unable to pay its debts as per the scheme, it may make an order for winding up the company and such an order shall be deemed to be an order made under section 273.
- (3) **Retrospective effect of order:** The provisions of this section shall, so far as may be, also apply to a company in respect of which an order has been made before the commencement of this Act sanctioning a compromise or an arrangement.

Powers of Tribunal to enforce compromise or arrangement sanctioned u/s 230 [Section 231]	Power to supervise the implementation of sanctioned compromise or arrangement.
	Power to give necessary directions or make necessary modifications in the compromise or arrangement, if required for its proper implementation .
	Power to make an order for winding up if compromise or arrangement cannot be implemented satisfactorily and the company is unable to pay its debts as per the Scheme.

The National Company Law Tribunal, New Delhi Bench, in *Tata Teleservices (Maharashtra) Ltd., In re*, under Section 231, read with sections 231 and 232, of the Companies Act, 2013 laid down that where all statutory compliance had been completed, scheme of arrangements was to be approved.

As per the facts, Telecommunication companies Bharti Airtel (resulting company) and Tata Teleservices (demerged company) sought for sanction of composite scheme of arrangement. Newspaper publication as directed by Tribunal in first motion application was effectively complied. Objection raised by unsecured creditor and shareholder was dismissed on the ground of having no locus as objectors were not meeting mandatory minimum threshold of 5 per cent prescribed in section 230 (4) of the Companies Act, 2013. Regional Director, Ministry of Corporate Affairs, Department of Income-tax and Department of Telecommunication had approved arrangement/scheme. Terms of composite scheme indicated that resulting company undertook to comply with terms/conditions, guidelines for transfer/merger and it further undertook to meet tax liabilities, debts, dues and obligations of demerged company. Accounting treatment proposed in scheme was in conformity with Accounting Standards specified in section 133 of the Companies Act, 2013. Members/creditors of resulting company had also approved the scheme in question. No investigation or proceedings were pending against these companies. Considering, since all statutory compliances had been fulfilled, it was held that impugned scheme of arrangements was to be approved and appropriate directions were to be issued.



4. MERGER AND AMALGAMATION OF COMPANIES [SECTION 232]

Section 232 of Companies Act, 2013 empowers NCLT to order merger or amalgamation. The provisions are detailed out below:

(1) **Filing of an application for purpose of reconstruction of companies involving merger/ amalgamation or transfer of undertaking, property etc. [Sub-section (1)]:**

Where an application is made to the Tribunal under section 230 for the sanctioning of a compromise or an arrangement proposed between a company and any such persons as are mentioned in that section, and it is shown to the Tribunal—

- (a) that the compromise or arrangement has been proposed for the purposes of, or in connection with, a scheme for the reconstruction of the company or companies involving merger or the amalgamation of any two or more companies; and
- (b) that under the scheme, the whole or any part of the undertaking, property or liabilities of any company (hereinafter referred to as the transferor company) is required to be transferred to another company (hereinafter referred to as the transferee company), or is proposed to be divided among and transferred to two or more companies,

the Tribunal may on such application, order a meeting of the creditors or class of creditors or the members or class of members, as the case may be, to be called, held and conducted in such manner as the Tribunal may direct and the provisions of sub-sections (3) to (6) of section 230 shall apply *mutatis mutandis*.

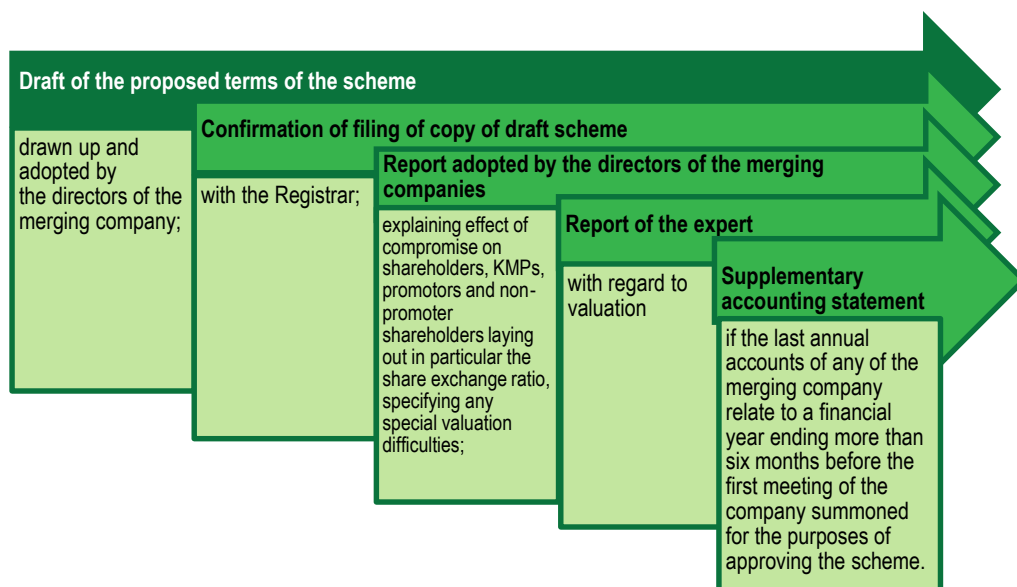
(2) **Circulation of information for the meeting by the merging companies / the companies in respect of which a division is proposed [Sub-section (2)]:**

Where an order has been made by the Tribunal as above, merging companies or the companies in respect of which a division is proposed, shall also be required to circulate the following for the meeting so ordered by the Tribunal, namely:—

- (a) the **draft** of the proposed terms of the scheme drawn up and adopted by the Directors of the merging company;
- (b) confirmation that a copy of the draft scheme has been **filed** with the Registrar;
- (c) a **report** adopted by the Directors of the merging companies explaining effect of compromise on each class of shareholders, key managerial personnel, promoters and non-promoter shareholders laying out in particular the **share exchange ratio**, specifying any special valuation difficulties;
- (d) the report of the expert with regard to **valuation**, if any;

- (e) a supplementary accounting statement if the last annual accounts of any of the merging company relate to a financial year ending more than six months before the first meeting of the company summoned for the purposes of approving the scheme.

Merging companies or the companies in respect of which a division is proposed, shall circulate the following for the meeting:



(3) **Order of Tribunal on the agreement of compromise or arrangement [Sub-section (3)]:**

The Tribunal, after satisfying itself that the procedure specified in sub-sections (1) and (2) has been complied with, may, by order, sanction the compromise or arrangement or by a subsequent order, make provision for the following matters, namely:—

- (a) **the transfer to the transferee company** of the whole or any part of the undertaking, property or liabilities of the transferor company from a date to be determined by the parties unless the Tribunal, for reasons to be recorded by it in writing, decides otherwise;
- (b) **the allotment or appropriation by the transferee company** of any shares, debentures, policies or other like instruments in the company which, under the compromise or arrangement, are to be allotted or appropriated by that company to or for any person:

Provided that a transferee company shall not, as a result of the compromise or arrangement, hold any shares in its own name or in the name of any trust whether

on its behalf or on behalf of any of its subsidiary or associate companies and any such shares shall be cancelled or extinguished;

- (c) **the continuation by or against the transferee company of any legal proceedings** pending by or against any transferor company on the date of transfer;
- (d) **dissolution, without winding-up**, of any transferor company;
- (e) **the provision to be made for any persons who**, within such time and in such manner as the Tribunal directs, dissent from the compromise or arrangement;
- (f) **where share capital is held by any non-resident shareholder** under the foreign direct investment norms or guidelines specified by the Central Government or in accordance with any law for the time being in force, the allotment of shares of the transferee company to such shareholder shall be in the manner specified in the order;
- (g) **the transfer of the employees of the transferor company** to the transferee company;
- (h) **where the transferor company is a listed company and the transferee company is an unlisted company,—**
 - (A) the transferee company shall remain an unlisted company until it becomes a listed company;
 - (B) if shareholders of the transferor company decide to opt out of the transferee company, provision shall be made for payment of the value of shares held by them and other benefits in accordance with a pre-determined price formula or after a valuation is made, and the arrangements under this provision may be made by the Tribunal:

Provided that the amount of payment or valuation under this clause for any share shall not be less than what has been specified by the Securities and Exchange Board under any regulations framed by it;

- (i) **where the transferor company is dissolved**, the fee, if any, paid by the transferor company on its authorised capital shall be set-off against any fees payable by the transferee company on its authorised capital subsequent to the amalgamation; and
- (j) such **incidental, consequential and supplemental matters** as are deemed necessary to secure that the merger or amalgamation is fully and effectively carried out:

Provided that no compromise or arrangement shall be sanctioned by the Tribunal unless a **certificate by the company's auditor has been filed with the Tribunal** to the effect that the accounting treatment, if any, proposed in the scheme of compromise or arrangement is in conformity with the accounting standards prescribed under section 133.



(4) **Effect of an order of tribunal [Sub-section (4)]:**

Where an order under this section provides for the transfer of any property or liabilities, then, by virtue of the order, that property shall be transferred to the transferee company and the liabilities shall be transferred to and become the liabilities of the transferee company and any property may, if the order so directs, be freed from any charge which shall by virtue of the compromise or arrangement, cease to have effect.

(5) **Filing of certified copy of order with registrar [Sub-section (5)]:**

Every company in relation to which the order is made shall cause a certified copy of the order to be filed with the Registrar for registration **within thirty days** of the receipt of certified copy of the order.

(6) **Effective date specified in scheme [Sub-section (6)]:**

The scheme under this section shall clearly indicate an appointed date from which it shall be effective and the scheme shall be deemed to be effective from such date and not at a date subsequent to the appointed date.

(7) **Filing of duly certified statement of compliance of scheme with registrar [Sub-section (7)]:**

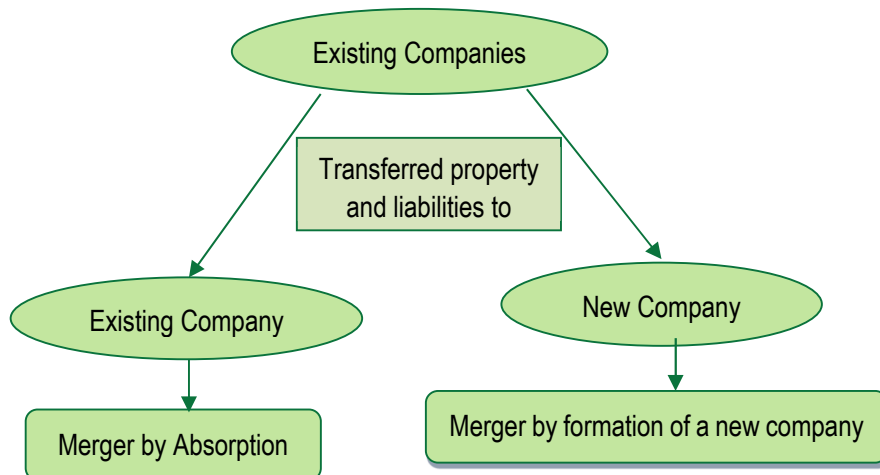
Every company in relation to which the order is made shall, until the completion of the scheme, file a statement in such form and within such time as may be prescribed with the Registrar every year duly certified by a chartered accountant or a cost accountant or a company secretary in practice indicating whether the scheme is being complied with in accordance with the orders of the Tribunal or not.

(8) **In case of contravention [Sub-section (8)]:**

If a company fails to comply with sub-section (5), the company and every officer of the company who is in default shall be liable to a penalty of twenty thousand rupees, and where the failure is a continuing one, with a further penalty of one thousand rupees for each day after the first during which such failure continues, subject to a maximum of three lakh rupees.

Explanation — For the purposes of this section,—

- (i) **in a scheme involving a merger**, where under the scheme the undertaking, property and liabilities of one or more companies, including the company in respect of which the compromise or arrangement is proposed, are to be transferred to another existing company, it is a **merger by absorption**, or where the undertaking, property and liabilities of two or more companies, including the company in respect of which the compromise or arrangement is proposed, are to be transferred to a new company, whether or not a public company, it is a **merger by formation of a new company**;



- (ii) **references to merging companies** are in relation to a merger by absorption, to the transferor and transferee companies, and, in relation to a merger by formation of a new company, to the transferor companies;
- (iii) **a scheme involves a division**, where under the scheme the undertaking, property and liabilities of the company in respect of which the compromise or arrangement is

proposed are to be divided among and transferred to two or more companies each of which is either an existing company or a new company; and

- (iv) **property includes** assets, rights and interests of every description and liabilities include debts and obligations of every description.

1. The National Company Law Tribunal of Chandigarh Bench in *Panasonic India (P.) Ltd., In re*, May 19, 2022 passed an order based on the principle that where proposed scheme of amalgamation between petitioner companies was for business consolidation and tax arrangements were merely a consequential fall out of implementation of scheme, it was to be sanctioned.

In the said case, the companies filed instant application under sections 230 to 232 seeking sanction of proposed scheme of amalgamation between them. Income-tax department raised objection against scheme on ground that there was huge accumulated loss in hands of Transferor Company and scheme was a vehicle to transfer accumulated losses to Transferee Company. It was held that since treatment of carrying forward and set-off of accumulated loss and unabsorbed depreciation allowance in amalgamation or demerger etc. of companies are clearly spelt out under section 72A and said issue could be examined at time of assessment of petitioner companies, there was no merit in objection of income-tax department. As proposed scheme was for business consolidation and tax arrangements were merely consequential fall out of implementation of scheme and scheme contemplated between petitioner companies appeared to be prima facie in compliance with requirement stipulated under relevant sections of the Companies Act, the proposed scheme was to be sanctioned.

2. The National Company Law Appellate Tribunal, New Delhi in *Ericsson India (P.) Ltd., In re*, laid down that where merger was of a wholly owned subsidiary company into its holding company, no shares would be allotted as consideration pursuant to merger; proposed scheme would not result in any dilution in shareholding of shareholders of transferee company and net worth of transferee company being positive, meeting of shareholders was to be dispensed with.



5. POWER TO ACQUIRE SHARES OF SHAREHOLDERS DISSENTING FROM SCHEME OR CONTRACT APPROVED BY MAJORITY [SECTION 235]

Section 235 of the Companies Act, 2013 contains provisions providing for acquiring of shares of shareholders dissenting from the scheme or contract approved by majority.

(1) Basic requirements as to acquisition of shares [Sub-section (1)]:

- **Approval by majority of shareholders:** The scheme or contract involving the transfer of shares or any class of shares in a company (the transferor company) to another company (the transferee company) has been **approved by the holders of not less than 9/10th in value of the shares** whose transfer is involved.

- **Time Limit for receiving approval:** The approval from 9/10th of the shareholders in value or more shall be received within **four months** after making of an offer in that behalf by the transferee company.
- **Acquisition of the remaining shares of dissenting shareholders:** The transferee company shall express its desire to acquire the remaining shares of dissenting shareholders within **two months** after the expiry of the said four months and shall give notice in the prescribed manner *[as per Rule 26 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016, notice needs to be sent in Form No. CAA-14]* to any dissenting shareholder that it desires to acquire his shares. The shares already held at the date of the offer by Transferee Company, or by a nominee of the transferee company or its subsidiary companies shall not be counted for this purpose.

(2) Order of Tribunal to acquire shares of dissenting shareholders [Sub-section (2)]:

Where a notice under sub-section (1) is given, the transferee company shall, unless on an application made by the dissenting shareholder to the Tribunal, **within one month** from the date on which the notice was given and the Tribunal thinks fit to order otherwise, be entitled to and bound to acquire those shares on the terms on which, under the scheme or contract, the shares of the approving shareholders are to be transferred to the transferee company.

Explanation — “Dissenting shareholder” includes a shareholder who has not assented to the scheme or contract and any shareholder who has failed or refused to transfer his shares to the transferee company in accordance with the scheme or contract.

(3) Application by dissenting shareholders [Sub-section (3)]:

- Where a notice has been given by the transferee company **on an application made by the dissenting shareholder** and the Tribunal has not, made an order to the contrary (*i.e.* order made in favor of the company), the transferee company shall, on the expiry of one month from the date on which the notice has been given, or,
- if an application to the Tribunal by the dissenting shareholder is then pending (nothing is required to be done); after that **application has been disposed of**—
shall send a copy of the notice to the transferor company together with an instrument of transfer, to be executed on behalf of the shareholder by any person appointed by the transferor company and on its own behalf by the transferee company, and pay or transfer to the transferor company the amount or other consideration representing the price payable by the transferee company for the shares which that company is entitled to acquire,
- The **transferor company shall—**
 - thereupon register the transferee company as the holder of those shares; and
 - within one month of the date of such registration, inform the dissenting shareholders of the fact of such registration and of the receipt of the amount or

other consideration representing the price payable to them by the transferee company.

- (4) **Separate Bank account for disbursement to entitled shareholders [Sub-section (4)]:** Any sum received by the transferor company under this section shall be paid into a separate bank account, and any such sum and any other consideration so received shall be held by that company in trust for the several persons entitled to the shares in respect of which the said sum or other consideration were respectively received and **shall be disbursed to the entitled shareholders within sixty days.**

- (5) **Scheme/contract made before the commencement of Act[Sub-section (5)]:**

In relation to an offer made by a transferee company to shareholders of a transferor company before the commencement of this Act, this section shall have effect with the following modifications, namely:—

- (a) in sub-section (1), for the words “the shares whose transfer is involved other than shares already held at the date of the offer by, or by a nominee of, the transferee company or its subsidiaries,”, the words “the shares affected” shall be substituted; and
- (b) in sub-section (3), the words “together with an instrument of transfer, to be executed on behalf of the shareholder by any person appointed by the transferee company and on its own behalf by the transferor company” shall be omitted.

Example 2: Special Furnishings Limited, a company incorporated under the Companies Act, 2013 applied to the Tribunal for a scheme of arrangement under section 230 of the Companies Act, 2013. The Tribunal by way of an order approved the scheme of arrangement involving amalgamation with Flip Furnitures and Fixtures Limited under section 232 of the Act. After due formalities, the requisite number of shareholders gave the approval to become the shareholders of Flip Furnitures and Fixtures Limited under section 235 of the Act. However, some of the shareholders did not consent to become the shareholders of Flip Furnitures and Fixtures Limited. In this case specified legal procedure shall be followed by dissenting shareholders considering the notice which has been given by Flip Furnitures and Fixtures Limited to dissenting shareholders mentioning that it desires to acquire their shares.

As per the provisions of section 235 of the Act, where a notice by the transferee company has been given to dissenting shareholders that it desires to acquire their shares, the dissenting shareholders may make an application to the Tribunal within one month from the date on which the notice was given for the Tribunal to pass an order otherwise than the acquisition of shares by transferee company. Accordingly, the dissenting shareholders shall make an application to the Tribunal within a period of one month from the date of notice given by Flip Furnitures and Fixtures Limited to pass an order otherwise than the acquisition of shares by Flip Furnitures and Fixtures Limited.



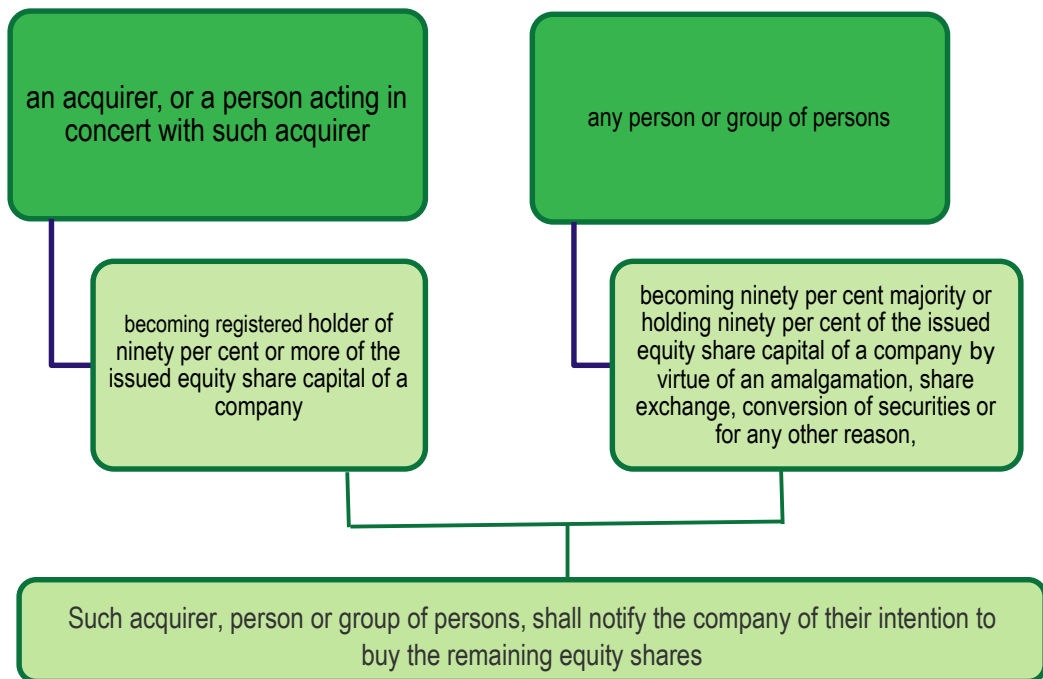
6. PURCHASE OF MINORITY SHAREHOLDING [SECTION 236]

The provisions of Section 236 of the Companies Act, 2013 deal with purchase of minority shareholding.

(1) Notifying company for purchase of minority shareholding [Sub-section (1)]:

- **In the event of an acquirer, or a person acting in concert with such acquirer** becoming registered holder of ninety per cent. or more of the issued equity share capital of a company, or
- **In the event of any person or group of persons** becoming ninety per cent. majority or holding ninety per cent. of the issued equity share capital of a company, by virtue of an amalgamation, share exchange, conversion of securities or for any other reason,

such acquirer, person or group of persons, as the case may be, shall notify the company of their intention to buy the remaining equity shares.



(2) Offer of equity shares to minority shareholders by acquirer, person or group of persons [Sub-section (2)]:

The acquirer, person or group of persons shall offer to the minority shareholders of the company for buying the equity shares held by such shareholders at a price determined on

the basis of valuation by a registered valuer in accordance with Rule 27 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016.

(3) **Offer to majority shareholder to purchase the minority equity shareholding [Sub-section (3)]:**

The minority shareholders of the company may offer to the majority shareholders to purchase the minority equity shareholding of the company at the price determined in accordance with Rule 27 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016.

(4) **Deposit of amount in separate bank account [Sub-section (4)]:**

The majority shareholders shall deposit an amount equal to the value of shares to be acquired by them under sub-section (2) or sub-section (3), as the case may be, in a separate bank account to be operated by the company whose shares are being transferred for at least one year for payment to the minority shareholders and such amount shall be disbursed to the entitled shareholders within sixty days:

Provided that such disbursement shall continue to be made to the entitled shareholders for a period of one year, who for any reason had not been made disbursement within the said period of sixty days or if the disbursement have been made within the aforesaid period of sixty days, fail to receive or claim payment arising out of such disbursement.

(5) **Company whose shares are being transferred to act as a transfer agent in the event of purchase [Sub-section (5)]:**

In the event of a purchase under this section, the company whose shares are being transferred shall act as a transfer agent for receiving and paying the price to the minority shareholders and for taking delivery of the shares and delivering such shares to the majority, as the case may be.

(6) **Company whose shares are being transferred to issue shares [Sub-section (6)]:**

In the absence of a physical delivery of shares by the shareholders within the time specified by the company,

- the share certificates shall be deemed to be cancelled, and
- the company whose shares are being transferred shall be authorised to issue shares in lieu of the cancelled shares and complete the transfer in accordance with law, and
- make payment of the price out of deposit made under sub-section (4) by the majority in advance to the minority by despatch of such payment.

(7) **Right of shareholders to make an offer for sale of minority equity shareholding [Sub-section (7)]:**

In the event of a majority shareholder or shareholders requiring a full purchase and making payment of price by deposit with the company for-

- any shareholder or shareholders who have died or ceased to exist, or
- whose heirs, successors, administrators or assignees have not been brought on record by transmission,

the right of such shareholders to make an offer for sale of minority equity shareholding shall continue and be available for a period of three years from the date of majority acquisition or majority shareholding.

(8) **Sharing of additional compensation [Sub-section (8)]:**

Where the shares of minority shareholders have been acquired in pursuance of this section, and as on or prior to the date of transfer following such acquisition, the shareholders holding seventy-five per cent. or more minority equity shareholding negotiate or reach an understanding on a higher price for any transfer, proposed or agreed upon, of the shares held by them without disclosing the fact or likelihood of transfer taking place on the basis of such negotiation, understanding or agreement,-

the majority shareholders shall share the additional compensation so received by them with such minority shareholders on a pro rata basis.

Explanation—For the purposes of this section, the expressions “acquirer” and “person acting in concert” shall have the meanings respectively assigned to them in clause (b) and clause (e) of sub-regulation (1) of regulation 2 of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 1997.

Example 3: The issued equity share capital of ABC Limited is INR 50 crore and 90% of such issued capital has been acquired by the XYZ Limited as a part of amalgamation. Out of remaining minority shareholding of INR 5 crore, share worth INR 4 crore are held by Mr. “A”. Hence, if he negotiates with the company a price higher than that decided under the scheme, the extra amount / compensation received by Mr. “A” shall be allocated to all minority shareholders on *pro-rata* basis.

(9) **Determination of price for purchase of minority shareholders:**

Rule 27 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 prescribes that the registered valuer shall determine the price to be paid by the acquirer, person or group of persons referred to in sub-section (1) of section 236 of the Act for purchase of equity shares of the minority shareholders of the company in accordance with the prescribed rules.

(10) **On failure of acquisition of shares [Sub-section (9)]:**

When a shareholder or the majority equity shareholder fails to acquire full purchase of the shares of the minority equity shareholders, then, the provisions of this section shall continue to apply to the residual minority equity shareholders, even though,—

- (a) the shares of the company of the residual minority equity shareholder had been delisted; and

- (b) the period of one year or the period specified in the regulations made by the Securities and Exchange Board under the Securities and Exchange Board of India Act, 1992, had elapsed.

Example 4: Ram Software Developers Limited, a company incorporated under the Companies Act, 2013 has paid up equity share capital of ₹ 1,00,00,000 (face value of ₹ 10 each divided into 10,00,000 shares). The company's financial position is gradually deteriorating since last 3 years. Rajan Software Limited, which is in the same line of business as that of Ram Software Developers Limited, has paid up equity share capital of ₹ 5,00,00,000 divided into 5,00,00,000 equity shares of Re. 1 each. It has proposed to take over Ram Software Developers Limited.

In order to complete the amalgamation in the nature of merger, minimum shareholders who are required to become the shareholders of Rajan Software Limited shall be such shareholders who hold shares not less than 90% in value of Ram Software Developers Limited.

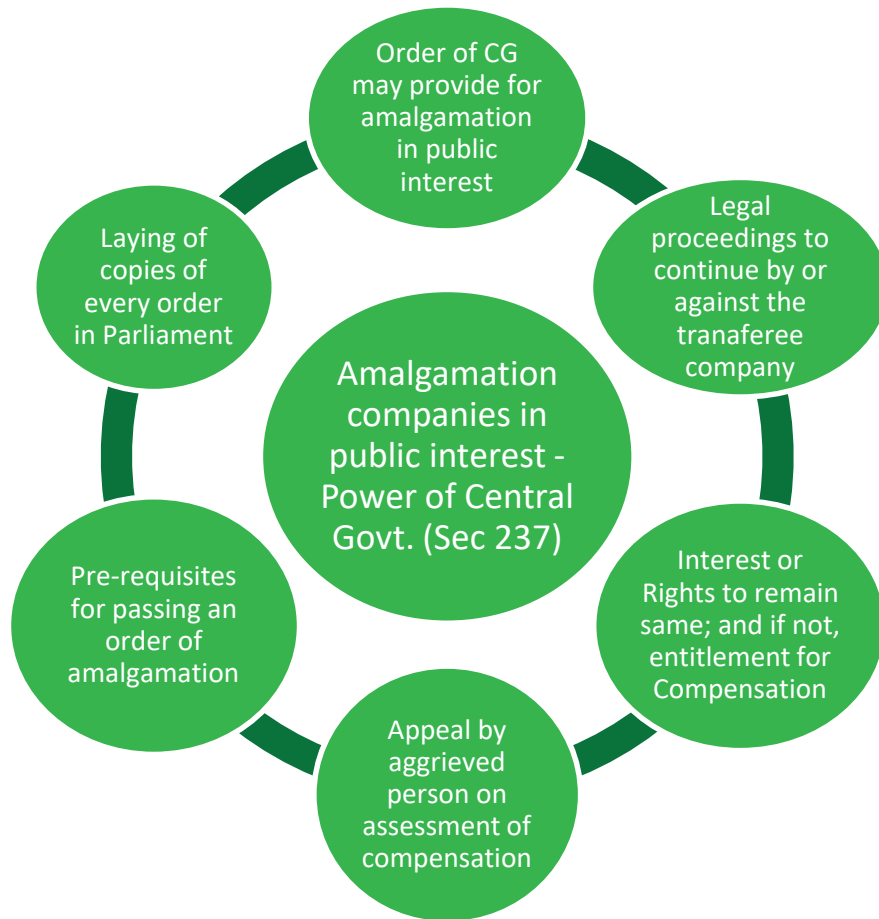
The National Company Law Appellate Tribunal, New Delhi, in *S. Gopakumar Nair v. OBO Bettermann India (P.) Ltd.* held that where majority shareholders of company purchased shareholding of minority shareholders at an agreed price to be decided by mutually acceptable Chartered Accountant and did not get it valued from registered valuer, same was in violation of provisions of section 236.

In the given case, Respondent 2 was holding 76 per cent shareholding in Respondent 1 company. Appellants, the minority shareholders filed oppression and mismanagement petition against respondents alleging that Respondent 2 made attempts to buy out their minority shareholdings and when they did not respond, Respondent 2 issued notices under section 236 and went ahead to buy shares of appellants in spite of their resistance. It was noted that section 236 (2) provides that offer to minority shareholders of company for buying equity shares held by said shareholders has to be at a price determined on basis of valuation by a registered valuer. Admittedly, Respondent 2 issued notice to appellants to sell their shares at agreed price to be decided by mutually acceptable Chartered Accountant and did not get it valued from registered valuer. It was thus held that notice given to appellants under section 236 and subsequent act of cancelling shares of appellants were illegal and was to be set aside.



7. POWER OF CENTRAL GOVERNMENT TO PROVIDE FOR AMALGAMATION OF COMPANIES IN PUBLIC INTEREST [SECTION 237]

Section 237 of the Companies Act, 2013 states the power of Central Government to provide for Amalgamation of companies in public interest.



(1) **Central Government may by order provide for amalgamation in public interest [Sub-section (1)]:**

Where the Central Government is satisfied that it is essential in the public interest that two or more companies should amalgamate, the Central Government may, by order notified in the Official Gazette, provide for the amalgamation of those companies into a single company with such constitution, with such property, powers, rights, interests, authorities and privileges, and with such liabilities, duties and obligations, as may be specified in the order.

(2) **Continuation of any legal proceedings by or against the transferee company [Sub-section (2)]:**

The order may also provide for the continuation by or against the transferee company of any legal proceedings pending by or against any transferor company and such consequential, incidental and supplemental provisions as may, in the opinion of the Central Government, be necessary to give effect to the amalgamation.

(3) **Interest or Rights to remain same; and if not, entitlement for Compensation [Sub-section (3)]:**

Every member or creditor, including a debenture holder, of each of the transferor companies before the amalgamation shall have, as nearly as may be, the same interest in or rights against the transferee company as he had in the company of which he was originally a member or creditor, and in case the interest or rights of such member or creditor in or against the transferee company are less than his interest in or rights against the original company, he shall be entitled to compensation to that extent, which shall be assessed by such authority as may be prescribed and every such assessment shall be published in the Official Gazette, and the compensation so assessed shall be paid to the member or creditor concerned by the transferee company.

(4) **Appeal by aggrieved person on assessment of compensation [Sub-section (4)]:**

Any person aggrieved by any assessment of compensation made by the prescribed authority under sub-section (3) may, within a period of thirty days from the date of publication of such assessment in the Official Gazette, prefer an appeal to the Tribunal and thereupon the assessment of the compensation shall be made by the Tribunal.

(5) **Pre-requisites for passing an order of amalgamation [Sub-section (5)]:**

No order shall be made under this section unless—

- (a) a copy of the **proposed order has been sent in draft** to each of the companies concerned;
- (b) the **time for preferring an appeal** under sub-section (4) has expired, or where any such appeal has been preferred, the appeal has been **finally disposed off**; and
- (c) the Central Government has considered, and made such **modifications**, if any, in the **draft order** as it may deem fit in the light of suggestions and objections which may be received by it from any such company within such period as the Central Government may fix in that behalf, not being less than two months from the date on which the copy aforesaid is received by that company, or from any class of shareholders therein, or from any creditors or any class of creditors thereof.

(6) **Copies of every order to be laid in Parliament [Sub-section (6)]:**

The copies of every order made under this section shall, as soon as may be after it has been made, be laid before each House of Parliament.



8. REGISTRATION OF OFFER OF SCHEMES INVOLVING TRANSFER OF SHARES [SECTION 238]

The provisions of Section 238 of the Companies act, 2013 provide for registration of offer of schemes involving transfer of shares.

(1) **Registration of circular / offer involving transfer of shares [Sub-section (1)]:**

In relation to every offer of a scheme or contract involving the transfer of shares or any class of shares in the transferor company to the transferee company under section 235,—

- (a) **every circular containing such offer and recommendation** to the members of the transferor company by its directors to accept such offer shall be accompanied by such information and in such manner as prescribed in Rule 28 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016;
- (b) **every such offer** shall contain a statement by or on behalf of the transferee company, disclosing the steps it has taken to ensure that necessary cash will be available; and
- (c) **every such circular shall be presented to the Registrar** for registration and no such circular shall be issued until it is so registered:

Provided that the Registrar may refuse, for reasons to be recorded in writing, to register any such circular which does not contain the information required to be given under clause (a) or which sets out such information in a manner likely to give a false impression, and communicate such refusal to the parties within **thirty days** of the application.

- (2) **Appeal against the order of the Registrar [Sub-section (2)]:** An appeal shall lie to the Tribunal against an order of the Registrar refusing to register any circular under sub-section (1).

(3) **Penalty for non-registration [Sub-section (3)]:**

The director who issues a circular which has not been presented for registration and registered under clause (c) of sub-section (1), shall be liable to a penalty of one lakh rupees.



9. PRESERVATION OF BOOKS AND PAPERS OF AMALGAMATED COMPANIES [SECTION 239]

According to Section 239 of the Companies Act, 2013, the books and papers of a company which has been amalgamated with, or whose shares have been acquired by, another company under this Chapter shall **not be disposed of without the prior permission of the Central Government** and before granting such permission, that Government may **appoint a person to examine** the books and papers or any of them for the purpose of ascertaining whether they contain any evidence of the commission of an offence in connection with the promotion or formation, or the management of the affairs, of the transferor company or its amalgamation or the acquisition of its shares.



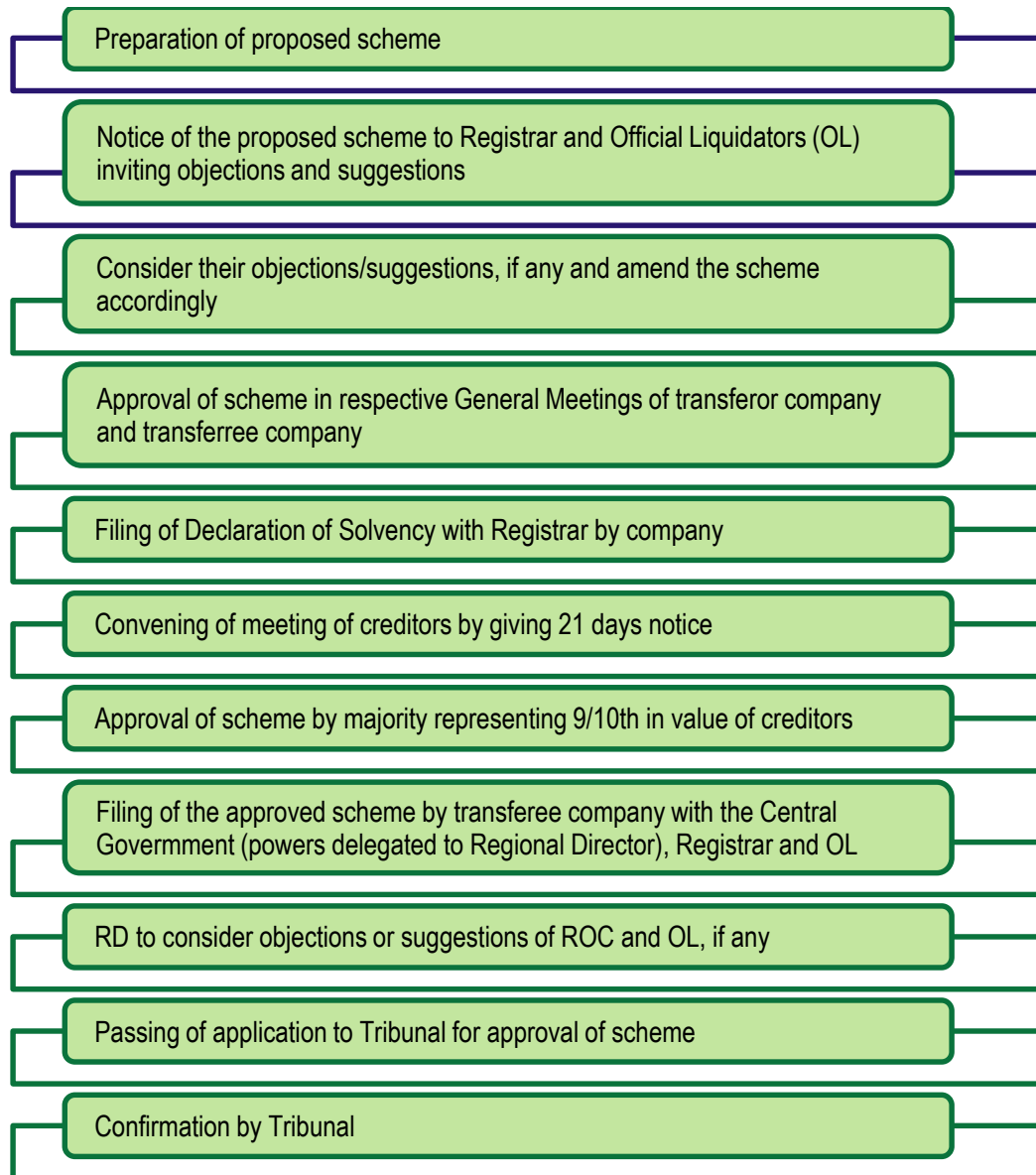
10. LIABILITY OF OFFICERS IN RESPECT OF OFFENCES COMMITTED PRIOR TO MERGER, AMALGAMATION, ETC. [SECTION 240]

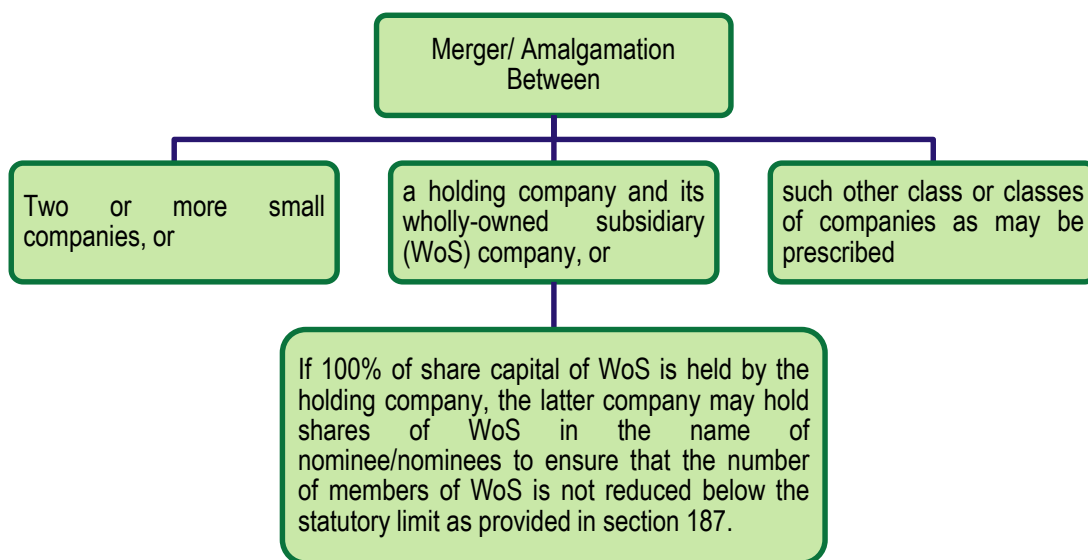
Retrospective effect of liability: Section 240 of the Companies Act, 2013 states that notwithstanding anything in any other law for the time being in force, the liability in respect of offences committed under this Act by the officers in default, of the transferor company prior to its merger, amalgamation or acquisition **shall continue after such merger, amalgamation or acquisition.**



11. FAST TRACK MODE OF MERGER OR AMALGAMATION OF CERTAIN COMPANIES [SECTION 233]

Overview of Section 233 of the Companies Act, 2013 is given below:





(1) **Companies who may enter into scheme of merger or amalgamation [Sub-section (1)]:**

A scheme of merger or amalgamation may be entered into between two or more small companies or between a holding company and its wholly-owned subsidiary company or class or classes of companies *i.e.*, between two or more start-up companies or one or more start-up company with one or more small company [given in Rule 25 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016].

Explanation- For the purposes of this sub-rule, “start-up company” means a private company incorporated under the Companies Act, 2013 or Companies Act, 1956 and recognised as such in accordance with notification number G.S.R. 127 (E), dated the 19th February, 2019 issued by the Department for Promotion of Industry and Internal Trade.

A scheme of merger or amalgamation may be entered, subject to following conditions:

- (a) a **notice of the proposed scheme inviting objections or suggestions**, if any, from the Registrar and Official Liquidators where registered office of the respective companies are situated or persons affected by the scheme within thirty days is issued by the transferor company or companies and the transferee company;
- (b) the **objections and suggestions received are considered by the companies** in their respective general meetings and the scheme is approved by the respective members or class of members at a general meeting holding at least ninety per cent. of the total number of shares;
- (c) each of the companies involved in the merger files a **declaration of solvency**, in the prescribed form, with the Registrar of the place where the registered office of the company is situated; and

- (d) the **scheme is approved by majority** representing nine-tenths in value of the creditors or class of creditors of respective companies indicated in a meeting convened by the company by giving a notice of twenty-one days along with the scheme to its creditors for the purpose or otherwise approved in writing.

(2) **Filing of copy of scheme with the Central Government, Registrar and the Official Liquidators [Sub-section (2)]:**

The transferee company shall file a copy of the scheme so approved in the manner as may be prescribed, with the Central Government, Registrar and the Official Liquidators where the registered office of the company is situated.

(3) **Approval or Rejection of scheme [Sub-sections (3) and (4)]:**

On the receipt of the scheme if the Registrar or the Official Liquidator has no objections or suggestions to the scheme, the Central Government shall register the same and issue a confirmation thereof to the companies.

If the Registrar or Official Liquidator has any objections or suggestions, he may communicate the same in writing to the Central Government within a period of **thirty days**.

If no such communication is made, it shall be presumed that he has no objection to the scheme.

(4) **Filing of application by Central government with Tribunal [Sub-section (5)]:**

If the Central Government after receiving the objections or suggestions or for any reason is of the opinion that such a scheme is not in public interest or in the interest of the creditors, it may file an application before the Tribunal **within a period of sixty days of the receipt of the scheme**, stating its objections and requesting that the Tribunal may consider the scheme under section 232.

(5) **Passing of an order of Tribunal [Sub-section (6)]:**

On receipt of an application from the Central Government or from any person, if the Tribunal, for reasons to be recorded in writing, is of the opinion that the scheme should be considered as per the procedure laid down in section 232, the Tribunal may direct accordingly or it may confirm the scheme by passing such order as it deems fit:

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

(6) **Communication of order to Registrar [Sub-section (7)]:**

A copy of the order confirming the scheme shall be communicated to the Registrar having jurisdiction over the transferee company and the persons concerned and the Registrar shall register the scheme and issue a confirmation thereof to the companies and such confirmation shall be communicated to the Registrars where transferor company or companies were situated.

(7) **Dissolution of transferor company [Sub-section (8)]:**

The registration of the scheme, shall be deemed to have the effect of dissolution of the transferor company without process of winding-up.

(8) **Effect of Registration of Scheme [Sub-section (9)]:**

The registration of the scheme shall have the following effects, namely:—

(a) **transfer of property or liabilities of the transferor company to the transferee company** so that the property becomes the property of the transferee company and the liabilities become the liabilities of the transferee company;

(b) the **charges**, if any, on the property of the transferor company shall be applicable and enforceable as if the charges were on the property of the transferee company;

(c) **legal proceedings** by or against the transferor company pending before any court of law shall be continued by or against the transferee company; and

(d) where the scheme provides for purchase of shares held by the dissenting shareholders or settlement of debt due to dissenting creditors, such amount, to the extent it is unpaid, shall become the **liability of the transferee company**.

Effect of Registration of Scheme

transfer of property or liabilities of the transferor company to the transferee company;

the charges, if any, on the property of the transferor company shall be applicable to and enforceable against the transferee company;

legal proceedings by or against the transferor company pending before any court of law shall be continued by or against the transferee company; and

where the scheme provides for purchase of shares held by the dissenting shareholders or settlement of debt due to dissenting creditors, such amount, to the extent it is unpaid, shall become the liability of the transferee company.

(9) **Effect of merger and amalgamation on transferee company [Sub-section (10)]:**

A transferee company shall not on merger or amalgamation, hold any shares in its own name or in the name of any trust either on its behalf or on behalf of any of its subsidiary or associate company and all such shares shall be cancelled or extinguished on the merger or amalgamation.

(10) **Filing of application by transferee company with the Registrar [Sub-section (11)]:**

The transferee company shall file an application with the Registrar along with the scheme registered, indicating the revised authorised capital and pay the prescribed fees due on revised capital:

Provided that the fee, if any, paid by the transferor company on its authorised capital prior to its merger or amalgamation with the transferee company shall be set-off against the fees payable by the transferee company on its authorised capital enhanced by the merger or amalgamation.

(11) **Applicability of the provisions [Sub-section (12)]:** The provisions of this section shall *mutatis mutandis* apply to-

- a company or companies specified in sub-section (1) in respect of a scheme of compromise or arrangement referred to in section 230, or
- division or transfer of a company referred to clause (b) of subsection (1) of section 232.

(12) The Central Government may provide for the merger or amalgamation of companies in such manner as may be prescribed. **[Sub-section (13)]**(13) A company covered under this section may use the provisions of section 232 for the approval of any scheme for merger or amalgamation. **[Sub-section (14)]**

(14) According to sub-rule (8) of Rule 25 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016, it is clarified that with respect to schemes of arrangements or compromise falling within the purview of section 233 of the Act, the concerned companies may, at their discretion, opt to undertake such schemes under sections 230 to 232 of the Act, including where the condition prescribed in clause (d) of sub-section (1) of section 233 of the Act has not been met.

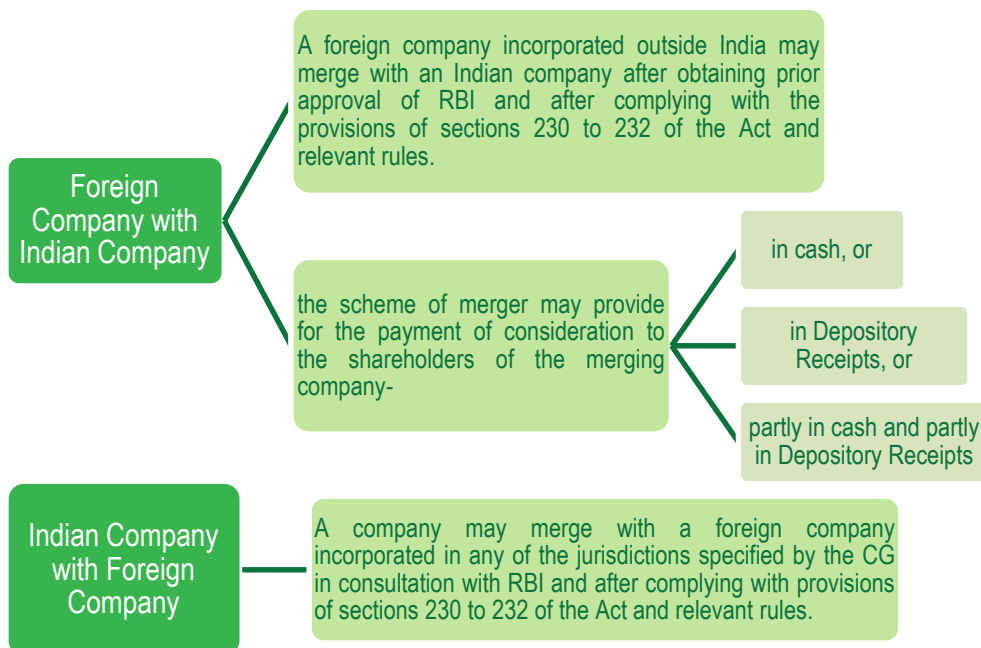


12. MERGER OR AMALGAMATION OF COMPANY WITH FOREIGN COMPANY [SECTION 234]

Section 234 of Companies Act, 2013 makes provisions in respect of cross border mergers and amalgamations *i.e.* between Indian company and a foreign body corporate.

Procedure has been prescribed in rule 25A of Companies (Compromises, Arrangements and Amalgamations) Rules, 2016.

The expression “**foreign company**” means ‘any company or body corporate incorporated outside India whether having a place of business in India or not.’



The National Company Law Tribunal, Ahmedabad Bench in *Sun Pharmaceutical Industries Ltd., In re*, laid that Compromise / arrangement / demerger of Indian companies with foreign company and vice versa is not permitted.

In the instant case, NCLT gave the decision as per Section 234 of the Companies Act, 2013, read with rule 25A of Companies (Compromise, Arrangements and Amalgamations) Rules, 2016. Here the Petitioner, a leading pharmaceutical company filed a petition seeking sanction of scheme of arrangement in nature of demerger and transfer of its 'Specified Investment Undertakings' to two overseas companies which were directly and indirectly wholly owned subsidiary of petitioner company. It was noted that provision of section 234 did not permit 'compromise' and/or 'arrangement' and/or 'demerger' of Indian companies with foreign company and vice versa. Further Rule 25A of Companies Rules in which detailed procedure and requirements were enumerated with respect to cross border mergers, was silent on 'demergers' and mentions only 'merger' and 'amalgamation'. Thus, it was held that instant petition for sanction of scheme of arrangement was to be disallowed.

TEST YOUR KNOWLEDGE**Multiple Choice Questions**

1. Sectoral Regulators shall make representation, if any, within _____ from the date of receipt of Notice of the Meeting to be called, held and conducted by the National Company Law Tribunal (NCLT) in respect of a scheme of compromise or arrangement.
 - (a) 45 days.
 - (b) 30 days.
 - (c) 60 days.
 - (d) 90 days.
2. It is imperative that the Scheme of Compromise or Arrangement needs to be approved by the members or class of members or creditors or class of creditors. From the given options, select the one which correctly indicates the minimum requirement for such approval:
 - (a) The Scheme of Compromise or Arrangement shall be approved by more than 50% majority in number of members or class of members or creditors or class of creditors, as the case may be, who are present and voting at the meeting.
 - (b) The Scheme of Compromise or Arrangement shall be approved by more than 75% majority in value of members or class of members or creditors or class of creditors, as the case may be, who are present and voting at the meeting.
 - (c) The Scheme of Compromise or Arrangement shall be approved by more than 75% majority in number of members or class of members or creditors or class of creditors, as the case may be, who are present and voting at the meeting.
 - (d) Both (a) and (b) together.
3. Mr. Aman is a registered holder of 15,000 equity shares of Kanha Textiles Limited whose issued capital is ₹ 1,00,00,000 divided into 10,00,000 equity shares of ₹ 10 each. He was offered a price, as determined by the registered valuer, for purchase of his shares by the majority shareholders. Since he has agreed to the proposal of selling his shares at the offered price, you are required to select the correct option from those given below that indicates the period within which such amount shall be disbursed to him:
 - (a) Maximum within 15 days, such offered amount shall be disbursed to him.
 - (b) Maximum within 30 days, such offered amount shall be disbursed to him.
 - (c) Maximum within 60 days, such offered amount shall be disbursed to him.
 - (d) Maximum within 90 days, such offered amount shall be disbursed to him.

4. Navneet Textiles Limited, with a view to save itself from the looming liquidation, proposed a scheme of compromise to its creditors which valued ₹ 75,00,000. In the process, the company filed the said Scheme with the jurisdictional National Company Law Tribunal (NCLT). From the following options, select the one which correctly depicts the minimum strength of creditors in value that must confirm to the scheme of compromise so that Tribunal may dispense with calling of a meeting of the creditors:
- The strength of creditors in value of Navneet Textiles Limited that must confirm to the scheme of compromise so that Tribunal may dispense with calling of a meeting of the creditors is minimum 70%.
 - The strength of creditors in value of Navneet Textiles Limited that must confirm to the scheme of compromise so that Tribunal may dispense with calling of a meeting of the creditors is minimum 80%.
 - The strength of creditors in value of Navneet Textiles Limited that must confirm to the scheme of compromise so that Tribunal may dispense with calling of a meeting of the creditors is minimum 90%.
 - The strength of creditors in value of Navneet Textiles Limited that must confirm to the scheme of compromise so that Tribunal may dispense with calling of a meeting of the creditors is minimum 95%.
5. In respect of a scheme of compromise submitted by Neon Colour Prints Limited to the jurisdictional National Company Law Tribunal (NCLT), a meeting of the shareholders was held on the specified date and time and at the designated place. The company had 1200 shareholders holding equity shares of ₹ 1,20,00,000 (12,00,000 equity shares of ₹ 10 each) who all voted using the prescribed modes. However, 100 shareholders holding ₹ 36,00,000 worth of shares voted against the approval of the scheme of compromise. Choose the correct option from those stated below as to whether the scheme of compromise submitted by Neon Colour Prints Limited to the jurisdictional National Company Law Tribunal (NCLT) is to be considered as approved or not:
- The scheme of compromise submitted by Neon Colour Prints Limited to the jurisdictional National Company Law Tribunal (NCLT) is to be considered as approved since shareholders holding more than one-half worth of shares in value voted in favour of the scheme.
 - The scheme of compromise submitted by Neon Colour Prints Limited to the jurisdictional National Company Law Tribunal (NCLT) is to be considered as approved since shareholders holding more than fifty-five percent worth of shares in value voted in favour of the scheme.
 - The scheme of compromise submitted by Neon Colour Prints Limited to the jurisdictional National Company Law Tribunal (NCLT) is to be considered as approved since

shareholders holding more than sixty percent worth of shares in value voted in favour of the scheme.

- (d) *The scheme of compromise submitted by Neon Colour Prints Limited to the jurisdictional National Company Law Tribunal (NCLT) is not to be considered as approved by the shareholders.*
6. *Orange Communications Limited is planning to merge with itself its Wholly-owned Subsidiary (WoS) Vaartalaap Tech Limited under the scheme of fast track merger. After due approval of the Merger Scheme, the same was filed with the Central Government for its approval. However, the Central Government is of the opinion that the said Merger Scheme is not in the public interest. In case such an opinion is formed, then with which authority the Central Government can file an application stating its objections?*
- (a) *The Central Government cannot file an application in this respect except to decide the matter on its own.*
 - (b) *The Central Government can file an application before the National Company Law Tribunal (NCLT) stating its objections.*
 - (c) *The Central Government can file an application before the Delhi High Court stating its objections.*
 - (d) *The Central Government can file a 'Special Leave Petition' before the Hon'ble Supreme Court stating its objections.*
7. *Abhik Trading and Marketing Company Limited is wholly owned subsidiary (WOS) of Eternal Cosmetics Limited. Keeping in view the expansion plans, Swapna and Shilpa, the two Directors of latter company are contemplating to make an application before the appropriate forum for merger of the subsidiary company Abhik Trading and Marketing Company Limited with holding company Eternal Cosmetics Limited under Section 232 of the Companies Act, 2013. However, Vibha Kumar, the Company Secretary of Eternal Cosmetics Limited is of the opinion that the merger between a holding and subsidiary company should have been undertaken as per the provisions of Section 233 which state procedure for fast track merger and not under Section 232. Which statement, out of the four given below, is applicable in the above stated situation:*
- (a) *The opinion of Vibha, the Company Secretary of the Eternal Cosmetics Limited, holds ground since merger between a holding and subsidiary company should have been undertaken as per the provisions of Section 233 of the Companies Act, 2013 which states procedure for fast track merger.*
 - (b) *The opinion of Vibha, the Company Secretary of the Eternal Cosmetics Limited, does not hold ground since merger between a holding and subsidiary company is validly possible only as per Section 232 of the Companies Act, 2013.*

- (c) The opinion of Vibha, the Company Secretary of the Eternal Cosmetics Limited, does not hold ground since the provisions given for fast track merger under Section 233 of the Companies Act, 2013 are of the optional nature.
- (d) The opinion of Vibha, the Company Secretary of the Eternal Cosmetics Limited, does not hold ground since the provisions given for fast track merger under Section 233 of the Companies Act, 2013 can be applied for merging only small companies.

Descriptive Questions

1. ABC Limited is a wholly owned subsidiary company of XYZ Limited. The Company wants to make application for merger of Holding and Subsidiary Companies under Section 232. The Company Secretary of the XYZ Limited is of the opinion that company cannot apply for merger as per section 232. The company shall have to apply for merger as per section 233 i.e. Fast Track Merger. Is it a valid contention expressed by the Company Secretary?
2. A meeting of members of ABC Limited was convened under the orders of National Company Law Tribunal (NCLT) to consider a scheme of compromise and arrangement. Notice of the meeting was sent in the prescribed manner to all the 600 members holding in the aggregate 25,00,000 shares. The meeting was attended by 450 members holding 15,00,000 shares. 210 members holding 11,00,000 shares voted in favour of the scheme. 180 members holding 3,00,000 shares voted against the scheme. The remaining members abstained from voting.
Examine with reference to the relevant provisions of the Companies Act, 2013 whether the scheme was approved by the requisite majority.
3. A meeting of members of DEF Limited was convened under the orders of the Court for the purpose of considering a scheme of compromise and arrangement. The meeting was attended by 300 members holding 10,00,000 shares. 120 members holding 7,00,000 shares in the aggregate voted for the scheme. 140 members holding 2,00,000 shares in aggregate voted against the scheme. 40 members holding 1,00,000 shares abstained from voting. *Examine with reference to the relevant provisions of the Companies Act, 2013 whether the scheme was approved by the requisite majority?*
4. At the meeting of the members of QRS Limited, a scheme of compromise and arrangement was approved by requisite majority. The National Company Law Tribunal (NCLT) after complying with the provisions, issued an Order, approving the scheme of compromise and arrangement.
List the matters to be provided in the Order issued by NCLT under Section 230 (7) of the Companies Act, 2013. Also state as to when shall the Order be filed with ROC?
5. A Ltd. (transferee company) decides to acquire B Ltd. (transferor company) by acquiring its shares via a process of takeover u/s 235 of the Companies Act, 2013. A Ltd. prepared a scheme by which an offer was made to the shareholders of B Ltd. The offer was made on 1st

August, 2019. The offer remained open for four months. Such offer was approved by shareholders having 92% value of the shares. Subsequently A Ltd. gave a notice to the remaining dissenting shareholders that it desires to acquire their shares. Such notice was given on 5th January, 2019. Certain dissenting shareholders made an application to the Tribunal that acquisition of their shares should not be permitted. However, their application was dismissed by the Tribunal. Hence A Ltd. acquired shares of 5% of the dissenting shareholders (out of balance 8%). The shareholding of balance 3% shareholders continued to remain with them. Comment on the validity of such a takeover by A Ltd.

ANSWERS

Answer to Multiple Choice Questions

1.	b	2.	d	3.	c	4.	c	5.	d
6.	b	7.	c						

Answer to Descriptive Questions

1. **As per section 233 (1)**, notwithstanding the provisions of section 230 and section 232, a scheme of merger or amalgamation may be entered between,

- Two or more small companies
- A holding company and its wholly-owned subsidiary company. If 100% of share capital of subsidiary company is held by the holding company, the latter company may hold the shares of subsidiary company in the name of any nominee or nominees with a view to ensure that the number of members of subsidiary company is not reduced below the statutory limit as mentioned in section 187.
- such other class or classes of companies as may be prescribed.

The provisions given for fast track merger in the section 233 are optional in nature and not mandatorily applicable to the company. If a company wants to make application for merger as per section 232, it can do so.

Hence, here the Company Secretary of the XYZ limited has erred in the law and his contention is not valid. The company shall have an option to choose between normal process of merger and fast track merger.

2. **As per section 230 (6)**, of the Companies Act, 2013 where majority of persons at a meeting held shares **representing 3/4th in value**, voting in person or by proxy or by postal ballot, agree to any compromise or arrangement and further such compromise or arrangement was sanctioned by the Tribunal by an order. The majority of persons representing 3/4th in value shall be counted considering the following:

- the creditors, or
- class of creditors or
- members or
- class of members, as the case may be,

The majority is dual, in number and in value. A simple majority of those voting is sufficient; whereas the 'three-fourths' requirement relates to value. The three-fourths value is to be computed with reference to paid-up capital held by members present and voting at the meeting.

In this case out of 600 members, 450 members attended the meeting, but only 390 members voted at the meeting. As 210 members voted in favour of the scheme the requirement relating to majority in number (i.e. 196) is satisfied. 390 members who participated in the meeting held 14,00,000, three-fourth of which works out to 10,50,000 while 210 members who voted for the scheme held 11,00,000 shares. As both the requirements are fulfilled, the scheme is approved by the requisite majority.

3. **As per section 230 (6)**, of the Companies Act, 2013 where majority of persons at a meeting held shares **representing 3/4th in value**, voting in person or by proxy or by postal ballot, agree to any compromise or arrangement and if such compromise or arrangement is sanctioned by the Tribunal by an order. The majority of persons representing 3/4th in value shall be counted considering the following:

- the creditors, or
- class of creditors or
- members or
- class of members, as the case may be,

The majority is dual, in number and in value. A simple majority of those voting is sufficient; whereas the 'three-fourths' requirement relates to value. The three-fourths value is to be computed with reference to paid-up capital held by members present and voting at the meeting.

In this case 300 members attended the meeting, but only 260 members voted at the meeting. As 120 members voted in favor of the scheme the requirement relating to majority in number (i.e. 131) is not satisfied.

260 members who participated in the meeting held 9,00,000 shares, three-fourth of which works out to 6,75,000 while 120 members who voted for the scheme held 7,00,000 shares. The majority representing three-fourths in value is satisfied.

Thus, in the instant case, the scheme of compromise and arrangement of DEF Limited is not approved as though the value of shares voting in favor is significantly more, the number of members voting in favor do not exceed the number of members voting against.

4. According to section 230(7) of the Companies Act, 2013, an order made by the Tribunal under sub-section (6) shall provide for all or any of the following matters, namely:—
- (a) where the compromise or arrangement provides for conversion of preference shares into equity shares, such preference shareholders shall be given an option to either obtain arrears of dividend in cash or accept equity shares equal to the value of the dividend payable;
 - (b) the protection of any class of creditors;
 - (c) if the compromise or arrangement results in the variation of the shareholders' rights, it shall be given effect to under the provisions of section 48;
 - (d) if the compromise or arrangement is agreed to by the creditors under sub-section (6), any proceedings pending before the Board for Industrial and Financial Reconstruction established under section 4 of the Sick Industrial Companies (Special Provisions) Act, 1985 shall abate;
 - (e) such other matters including exit offer to dissenting shareholders, if any, as are in the opinion of the Tribunal necessary to effectively implement the terms of the compromise or arrangement.

The order of the Tribunal shall be filed with the Registrar by the company within a period of thirty days of the receipt of the order. [Section 230(8)]

5. The basic requirements as to acquisition of shares mentioned in Section 235 of the Companies Act, 2013 are as follows:-
1. The scheme or contract involving the transfer of shares in a company (transferor company) to another company (transferee company) has been approved by the holders of not less than 9/10th (90%) in value of the shares whose transfer is involved.
 2. The approval of 9/10th shareholders in value shall be received within 4 months after making of an offer in that behalf by the transferee company.
 3. The transferee company shall express his desire to acquire the remaining shares of dissenting shareholder in 2 months after the expiry of the said 4 months and shall give notice in the prescribed manner to any dissenting shareholder that it desires to acquire his shares.

The transferee company shall be entitled as well as bound to acquire the shares of the dissenting shareholders where no application is made by any dissenting shareholders to the tribunal in 1 month of receipt of notice of acquisition of shares or where an application is made by any dissenting shareholder but such application is dismissed by the Tribunal.

In the given case, since application made by the dissenting shareholders has been dismissed by the Tribunal, A Ltd is bound to acquire all the shares of the dissenting shareholders *i.e.* entire 8% shareholding.

Since A Ltd acquired only 5% shareholding of the dissenting shareholders, this is in contravention of Section 235 of the Companies Act, 2013. Hence, the takeover of B Ltd. by A Ltd. is invalid.

[illegible]

CHAPTER

6

PREVENTION OF OPPRESSION AND MISMANAGEMENT



LEARNING OUTCOMES

By the end of this chapter, you would be able to :

- ☐ Describe actions which the NCLT might take into consideration to acknowledge the fact of oppression and mismanagement in a company.
- ☐ List the persons who have the right to file the application against oppression and mismanagement.
- ☐ Ascertain remedies available to aggrieved party in case of oppression or mismanagement
- ☐ Explain the provisions relating to Class Action Suits



1. INTRODUCTION

To begin with, let us understand the basic concept hidden behind this Chapter. Firstly, we should understand that the words “**Oppression**” & “**Mismanagement**” are two different concepts. Under the Companies Act, a question arises as to why would the company law even introduce such a Chapter, when all the provisions are crystal clear and explanatory? The answer to this question is “law evaders always find loopholes to their advantage”.

We may take an **example** to understand **oppression**. Let us imagine a situation where a company Rexagon Private Limited, has seven shareholders, namely, Mr. Abhishek, Mr. Archit, Mr. Ankur, Mr. Anupam, Mr. Himanshu, Mr. Manas and Mr. Rajan. Out of these, Mr. Abhishek, Mr. Archit and Mr. Ankur hold around 94% shares of the company. At the general meeting of Rexagon Private Limited when any resolution is required to be passed whether as ordinary or special, such resolution shall be passed in the favour of these three shareholders if they vote in the favour of resolution since they have majority shareholding of the company. Therefore, the voice of the minority shareholders *i.e.* Mr. Anupam, Mr. Himanshu, Mr. Manas and Mr. Rajan will be oppressed whether individually or jointly.

This is because the corporate law works on the principle of democracy and it becomes more vulnerable as it is reckoned with the number of shares and not with the number of individuals involved. This is known as the famous ‘**Rule of Majority**’ or which is also called the ‘**Foss v. Harbottle**’ Rule. It is a landmark judgement in the history of company law. It states that the ones who hold majority of shares “rule” the company (*Foss v. Harbottle (1843) 2 Hare 461*). The judgement held that if the majority shareholders have made a decision to take or not to take a certain action, it shall be respected. Also, the courts are not expected to ordinarily intervene to protect the minority interest affected by the resolutions passed by the majority.

Rule of majority

The case of *Foss v. Harbottle* is explained below:

In this case, two shareholders commenced legal action against the promoters and directors of the company alleging that they had misapplied the company’s assets and had improperly mortgaged the company’s property. The Court rejected the two shareholders’ plea and held that a breach of duty by the directors of the company was wrong done to the company for which it (*i.e.* the company) alone could sue. In other words, the proper plaintiff in that case was the company and not the two individual shareholders. Thus, the case of *Foss v. Harbottle* derives two major rules or principles of company law – first, a company is a legal entity separate from its shareholders; and second that the Court will not interfere with the internal management of companies acting within their powers. Therefore, where an ordinary majority of members can ratify the act, the Court will not interfere.

However, the said rule has four exceptions detailed as under:

- *Ultra-vires* or illegal acts;

- Transactions requiring special majorities;
- Personal Rights; and
- The “fraud on the minority”.

This Chapter focuses on the last exception *i.e.* “fraud on the minority” . As per the said exception, majority of shareholders cannot use their powers to defraud the minority. 'Fraud on minority' means taking of decisions and passing resolutions which would discriminate between majority shareholders and minority shareholders, so as to give an undue advantage to the majority shareholders.

For **Example** - majority shareholders are passing a resolution, purpose of which is to compulsory acquire the shares of minority shareholders though showing that such action will be advantageous to the company.

From the provisions of the Companies Act, 2013, it can be ascertained that legislative intent to safeguard the minority interest is quite comprehensive. The Companies Act, 2013 contains various rights applicable to such minority shareholders with a view to protect their interest in the company and also to address issues of abuse by the majority shareholders who control the companies. The Act also provides various benefits to the minority shareholders that were not provided under the old Act *i.e.*, under the Companies Act, 1956. Following are the rights and benefits of the minority shareholders:

- (1) **Right to appoint Small Shareholders' Director:** Section 151 enables small shareholders, who are also minority shareholders, to appoint a small shareholders' director in the company.
- (2) **Right to file an application to NCLT in cases of Oppression and Mismanagement:** Minority shareholders have right to move National Company Law Tribunal (NCLT) to report any acts of oppression and mismanagement by the board or management of the company. These rights are provided under Section 241 of the Act.
- (3) **Right to file a Class Action Suit:** The Companies Act, 2013 provides opportunity to minority shareholders to file a class action suits. Group of persons with a common interest may approach NCLT against the company, its board or the management.
- (4) **Right for Reconstruction and Amalgamation of Companies:** In specific, the Act, through Section 235 and 236 offers protection to the interests of minority shareholders. These sections deals with the concerns of interests of minority shareholders being suppressed in implementation of schemes of mergers, amalgamations and reconstruction.
- (5) **E-voting Process:** Through Section 108 of the Act, certain companies can offer e-voting facility to shareholders to vote at the meetings of on shareholders. This provision has empowered minority shareholders to exercise their voting rights without attending the meetings in person.
- (6) **Change of concept from majority rule to minority rule :** Section 188 of the Companies Act, 2013 which deals with related party transactions, mandates companies to undertake such transactions only after receiving approval from the majority of non-interested parties. Since majority

shareholders are usually the interested parties, the minority shareholders are naturally considered as non-interested parties. Hence, it is the minority shareholders that get to approve such transactions.

Rights and Benefits of Minority Shareholders

Right to appoint small shareholders' director

Right file application with NCLT in cases of oppression and mismanagement

Right to file Class Action Suit

Protection of interest in case of reconstruction, amalgamation and merger of companies

Emergence of e-voting

Change of concept from majority rule to minority rule

Chapter XVI of the Companies Act, 2013 covering sections 241 to section 246 relating to the provisions of protection to shareholders against oppression and mismanagement of those who are in control of the company.

Oppression

Let us understand the meaning of 'oppression' as used in the Act. The meaning of the term "oppression" as explained by Lord Cooper in the Scottish case of *Elder vs. Elder & Watson Ltd.* was cited with approval by Wanchoo J. of the Supreme Court of India in the case of *Shanti Prasad Jain vs. Kalinga Tubes*. He said that the conduct complained of, should at least involve a visible departure from the standards of their dealing and violations of conditions of fair play on which every shareholder who entrusts his money to company, is entitled to rely.

The complaining member must show that he is suffering from oppression in his capacity as a member but not in any other capacity.



To constitute oppression, persons concerned with the management of the company's affairs must, in connection thereof, be guilty of fraud, misfeasance or misconduct towards the members. It does not include mere domestic disputes between directors and members, or lack of confidence between one set of members and others.

It was observed in the case of *Rao (V.M.) vs. Rajeshwari Ramakrishnan* that the oppression complained off must affect a person in his capacity or character as a member of the company, harsh or unfair treatment in other capacity, e.g., as a director or a creditor is outside the purview of this chapter.

There must be a continuous acts constituting oppression up to the date of the petition.

The events have to be considered not in isolation but as a part of a continuous suffering.

The conduct complained of, can be said to be "oppression" only when it could be said that it is burdensome, harsh and wrongful; involves at least an element of lack of probity and fair dealing to a member in matters of his proprietary right as a shareholder.

How Act explained oppression and mismangement:

The Act defines that

- (i) **If affairs of a company** have been or are been conducted **prejudicial to public interest** or in a manner **prejudicial or oppressive to any member** or **prejudicial to the interest of company**, there is a case of oppression.
- (ii) **Any material change** that has taken place in **management or control of a company** and that by reason of such change it is likely that the **affairs of a company** will be conducted **prejudicial to interest of its member** or **company**, that would also be considered as mismanagement.



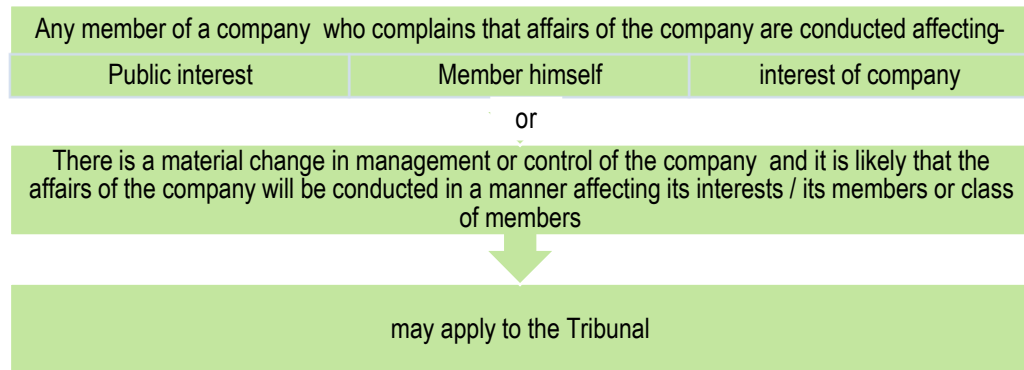
2. APPLICATION TO TRIBUNAL FOR RELIEF IN CASES OF OPPRESSION, ETC. [SECTION 241]

Section 241 of the Companies Act, 2013 states the circumstances in which an application may be made to the Tribunal by any member of a company or by the Central Government for relief from oppression and mismanagement.

- (1) **Right of member to apply to the Tribunal:** Any member of a company who complains that—
 - (a) the **affairs of the company** have been or are being conducted in a manner prejudicial to public interest or in a manner prejudicial or oppressive to him or any other member or members or in a manner prejudicial to the interests of the company; or
 - (b) the **material change**, not being a change brought about by, or in the interest of, any creditors, including debenture holders or any class of shareholders of the company,

has taken place in the management or control of the company, whether by an alteration in the Board of Directors or manager, or in the ownership of the company's shares, or if it has no share capital, in its membership, or in any other manner whatsoever, **and** that by any reason of such change, it is likely that the affairs of the company will be conducted in a manner prejudicial to its interest or its members or any class of members,

may apply to the Tribunal, provided such member has a right to apply under section 244, for an order under this Chapter.



Section 241(1) addresses complaints with respect to the conduct of the company's affairs, which could be prejudicial to public interest and prejudicial or oppressive to the members or the company itself.

The provision gives right to the members to move to the Tribunal not only in case of complaints of oppression but also in case of complaints that the conduct of the affairs of the company has been 'prejudicial' to them.

Section 241(1)(a) also provides for past acts of oppression.

This section also provides remedy for mismanagement in the affairs of the company. It states that a member may complain that "the affairs of a company are being conducted in a manner prejudicial to public interest or in a manner prejudicial to the interests of the company".

A member of a company may also complain in case there is a material change in the management and such change is likely to be prejudicial to the interests of the company or its members or any class of members.

Material change in the management may occur if there is:

- (a) an alteration in the Board of Directors or manager; or
- (b) an alteration in the ownership of the company's shares; or
- (c) an alteration in the membership, if the company has no share capital; or
- (d) an alteration in any other manner, whatsoever.

A change will not be considered material change if it has been brought about by, or in the interests of, any creditors, including debenture-holders or any class of shareholders of the company.

- (2) **Central Government may apply suo moto to the Tribunal:** The Central Government, if it is of the opinion that the **affairs of the company** are being conducted in a manner **prejudicial to public interest**, it may itself apply to the Tribunal for an order under this Chapter.

Provided that the applications under this sub-section, in respect of such company or class of companies, as may be prescribed, shall be made before the Principal Bench of the Tribunal which shall be dealt with by such Bench.

- (3) **Initiation of case by CG:** Where in the opinion of the Central Government there exist **circumstances** suggesting that—

- (a) **any person** concerned in the **conduct and management of the affairs of a company** is or has been in connection therewith **guilty of fraud, misfeasance, persistent negligence or default** in carrying out his obligations and functions under the law or of **breach of trust**;
- (b) the **business** of a company is **not or has not been conducted and managed** by such person in accordance **with sound business principles or prudent commercial practices**;
- (c) a **company** is or has been **conducted and managed by such person** in a manner which is likely to cause, or has caused, **serious injury or damage to the interest of the trade, industry or business** to which such company pertains; or
- (d) the **business** of a company is or has been **conducted and managed by such person** with **intent to defraud its creditors, members or any other person or otherwise for a fraudulent or unlawful purpose** or in a manner **prejudicial to public interest**,

the Central Government may initiate a case against such person and refer the same to the Tribunal with a request that the Tribunal may inquire into the case and record a decision as to whether or not such person is a fit and proper person to hold the office of director or any other office connected with the conduct and management of any company.

- (4) The person against whom a case is referred to the Tribunal under sub-section (3), shall be joined as a respondent to the application.
- (5) Every application under sub-section (3)-
 - (a) shall contain a concise statement of such circumstances and materials as the Central Government may consider necessary for the purpose of the inquiry; and
 - (b) shall be signed and verified in the manner laid down in the Code of Civil Procedure, 1908, for the signature and verification of a plaint in a suit by the Central Government.

Examples

1. In an application filed to the Tribunal, claiming oppression, a shareholder who is also the director of the company cannot claim compensation by way of salary paid to other directors. Shareholders can share the dividend of the company, if it is declared but cannot seek directions to be compensated. The payment of salary is a question that concerns the Board of Directors and not the Tribunal.
2. Failure to declare dividend does not amount to oppression. (*Thomas Veddon V.J. vs. Kuttanad Robber Co. Ltd.*).
3. A legal heir of a deceased shareholder filed a petition. Such legal heir was in the position of a minority shareholder. Can the application filed by the legal heir to the Tribunal, be maintainable in court?

Here, the legal heir of the deceased shareholder with minority status is entitled to file the petition even his name is not on the register of members of the company.
4. In a case where a person, without being so appointed, was acting as a Managing Director and discharging his functions with or without the knowledge of the members, a member can not file an application with the Tribunal claiming it as an act of oppression.
5. While obtaining relief from Tribunal, continuous losses cannot be regarded as oppression by itself (*Ashok Betelnut Co. P. Ltd. vs. M.K. Chandrakanth*).
6. Section 241 contains the words "Any member of a company who complains...." which implies that only a shareholder can seek remedy under section 242 by filing an application with Tribunal. In view of the wordings of Section 241, the Apex Court in *Tata Consultancy Services Ltd. v. Cyrus Investments (P) Ltd.* [(2021) 9 SCC 449] clarified that even a director's removal cannot be held to be oppressive / prejudicial.

The Supreme Court of India in *Mahima Datla vs. Dr. Renuka Datla* April 6, 2022 passed an order in the light of Section 241, read with section 242, of the Companies Act, 2013. According to the facts, an application was filed to Tribunal for relief. Here Respondent was director in a company which was started by her husband late 'V'. Respondent's case before CLB was that one 'X' having resigned from post of director of company had convened board meetings wherein appellants, daughters of 'V', were appointed as directors and shares standing in name of 'V' were transferred in favour of appellants although a will was executed by 'V' bequeathing all his shares in her favour.

Though, CLB had denied interim relief prayed for, High Court by impugned order held meeting of Board of Directors as null and void and set aside all resolutions passed therein. It also granted exclusive benefit of transmission of one fourth of disputed shares in favour of respondent.

Since 'X' had never seized to be a director as he had withdrawn his resignation prior to its acceptance, meetings conducted by 'X' were held valid.

Since issue related to inheritance of shares was subject matter of Civil Suit pending before Civil Court, it was held that High Court should not have dwelled into such issue and granted one fourth shares in favour of respondent. As no iota of evidence was placed by respondent that affairs of company were being conducted in a manner prejudicial to public interest, impugned order passed by High Court was held to be set aside.



3. RIGHT TO APPLY UNDER SECTION 241 [SECTION 244]

Section 244 of the Companies Act, 2013 is linked to section 241. It states the eligibility of members as to who all possess the right to file an application for oppression and mismanagement under Section 241 with the Tribunal. The eligibility criterion provided in section 244 ensures that only the persons with sufficient interest in the affairs of the company can file the petition under section 241 of the Act.

(1) Members having right to apply: The following members of a company shall have the right to apply under section 241, namely:—

(a) **In the case of a company having share capital-**

Members eligible to apply shall be the lowest of the following-

- 100 members; or
- 1/10th of the total members; or
- holding 1/10th of total issued share capital.

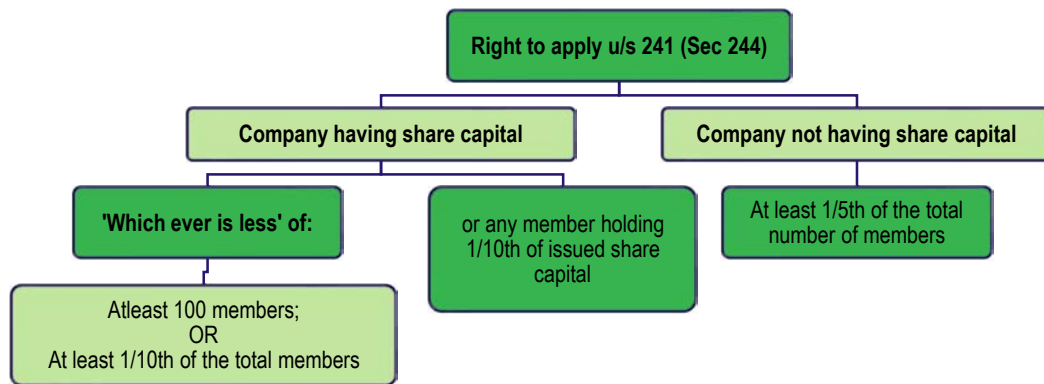
subject to the condition that the applicant or applicants has or have paid all calls and other sums due on their shares;

(b) **in the case of a company not having share capital-** at least 1/5th of the total number of its members:

Provided that on the application made to tribunal, The Tribunal may waive all or any of the requirements specified in clause (a) or clause (b) to enable the members to apply under section 241.

Explanation—For the purposes of this sub-section, where any share or shares are held by two or more persons jointly, they shall be counted only as one member.

(2) Entitlement to members to make an application: Any one or more members may make an application under subsection (1) to the Tribunal on behalf of all the members by obtaining the written consent of other member.



Examples

1. In a case of oppression where the shareholding of the petitioner has been reduced below 10 per cent due to fresh issue/allotment of shares, though the maintainability of the petition would be reduced after determining the validity of the issue of allotment but the petition shall still be maintainable and the petitioner shall be entitled to relief.
2. The requirement of shareholding upto the prescribed percentage is mandatory. It must be shown with the help of documentary evidences. Possession of share certificates is a prima facie proof that the petitioner is a shareholder. There is a presumption that a share certificate is a valid title to shares.
3. Shareholding and membership is reckoned not on the basis of the subscribed or paid-up share capital, but on the basis of the 'issued' share capital. For instance, a company may have issued a share capital of 50 lakh rupees divided into 50,000 shares of face value of 100 rupees each, but only 45,000 shares may have been subscribed for. The remaining shares will be left to be disposed of in such a manner as the Board of Directors think best in the interests of the company. 'Issued' share capital would include both equity and preference share capital.
4. The consent to be given by a shareholder is reckoned at the beginning of the proceedings. The withdrawal of consent by any shareholder during the course of proceedings shall not affect the maintainability of the petition [*Rajamundhry Electric Corporation Vs. V. Nageswar Rao A.I.R. (1956) Sc. 2013.*]
5. The National Company Law Tribunal, Chennai Bench in *John S. Dorai v. Church of South India Trust Association* held that where petitioner alleged that articles of association was illegally amended and some properties were sold away in respect of a charitable company, petition filed under section 241 was not maintainable as petitioner was neither a member nor a shareholder of said company.



4. POWERS OF TRIBUNAL [SECTION 242]

National Company Law Tribunal (NCLT) has been given wide powers under section 242 of Companies Act, 2013 to solve the matter judicially, on receipt of an application complaining oppression and mismanagement. NCLT will hear the matter and will pass suitable order. Procedure to be followed after NCLT issues order is also specified in section 242 of the Companies Act, 2013.

(1) Order passed by the Tribunal: If, on any application made under section 241, the Tribunal is of the opinion—

- (a) that the company's affairs have been or are being conducted in a manner prejudicial or oppressive to any member or members or prejudicial to public interest or in a manner prejudicial to the interests of the company; and
- (b) that to wind up the company would unfairly prejudice such member or members, but that otherwise the facts would justify the making of a winding-up order on the ground that it was just and equitable that the company should be wound up,

the Tribunal may, with a view to bringing to an end the matters complained of, make such order as it thinks fit.

(2) Nature of orders that can be passed by the Tribunal: Without prejudice to the generality of the powers under sub-section (1), an order under that sub-section may provide for—

- (a) the regulation of conduct of affairs of the company in future;
- (b) the purchase of shares or interests of any members of the company by other members thereof or by the company;
- (c) in the case of a purchase of its shares by the company as aforesaid, the consequent reduction of its share capital;
- (d) restrictions on the transfer or allotment of the shares of the company;
- (e) the termination, setting aside or modifications, of any agreement, how so ever arrived at, between the company and the managing director, any other director or manager, upon such terms and conditions as may, in the opinion of the Tribunal, be just and equitable in the circumstances of the case;
- (f) the termination, setting aside or modifications of any agreement between the company and any person other than those referred to in clause (e):

Provided that no such agreement shall be terminated, set aside or modified except after due notice and after obtaining the consent of the party concerned;

- (g) the setting aside of any transfer, delivery of goods, payment, execution or other act relating to property made or done by or against the company within three months before the date of the application made under this section, which would, if made or

done by or against an individual, be deemed in his insolvency to be a fraudulent preference;

- (h) removal of the managing director, manager or any of the director of the company;
- (i) recovery of undue gains made by any managing director, manager or director during the period of his appointment as such and the manner of utilisation of the recovery including transfer to Investor Education and Protection Fund or repayment to identifiable victims;
- (j) the manner in which the managing director or manager of the company may be appointed subsequent to an order removing the existing managing director or manager of the company made under clause (h);
- (k) appointment of such number of persons as directors, who may be required by the Tribunal to report to the Tribunal on such matters as the Tribunal may direct;
- (l) imposition of cost as may be deemed fit by the Tribunal;
- (m) any other matter for which, in the opinion of the Tribunal, it is just and equitable that provision should be made.

(3) Filing of copy of order of Tribunal: A certified copy of the order of the Tribunal, shall be filed by the company with the Registrar within 30 days of the order of the Tribunal.

(4) Interim order: The Tribunal may, on the application of any party to the proceeding, make any interim order which it thinks fit for regulating the conduct of the company's affairs upon such terms and conditions as appear to it to be just and equitable.

At the conclusion of the hearing of the case in respect of sub-section (3) of section 241, the Tribunal shall record its decision stating therein specifically as to whether or not the respondent is a fit and proper person to hold the office of director or any other office connected with the conduct and management of any company. [Sub-section 4A]

(5) Alteration in Memorandum or Articles through order of Tribunal: Where an order of the Tribunal makes any alteration in the memorandum or articles of a company, then, notwithstanding any other provision of this Act, the company shall not have power (except to the extent, if any, permitted in the order) to make, any alteration whatsoever which is inconsistent with the order, either in the memorandum or in the articles without the leave of the Tribunal. [Sub-section 5]

(6) Altered provision shall apply: The alterations made by the order in the memorandum or articles of a company shall have the same effect in all respects as if they had been duly made by the company in accordance with the provisions of this Act and the said provisions shall apply accordingly to the memorandum or articles so altered.

- (7) **Filing of certified copy of order altering the Memorandum or Articles with the Registrar:** A certified copy of every order altering, or giving leave to alter, a company's memorandum or articles, shall be filed by the company with the Registrar who shall register the same within 30 days after the making thereof.
- (8) **Punishment in case of contravention:** If a company contravenes the provisions of sub-section (5), the company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to twenty-five lakh rupees and every officer of the company who is in default shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees.

Examples

1. Mere lack of confidence among members themselves resulting in certain acts of irregularities or illegalities cannot be held to be oppressive per se. A case of oppression as well as mismanagement has to be made out by the petitioners substantiating that the acts complained of have caused prejudice to the interest of the company and its members and shareholders to have a cause of action to attract the provisions of the Act.
2. The matter of selection and appointment of dealers of the company's products, is not within the ambit and scope of the proceedings under section 241 (erstwhile section of the Act). In a tripartite agreement with the government, a project was assigned to the company. In this case, the right to manage the affairs of the company is vested in the majority of the shareholders and not in the person who might have procured the project for the company.
3. The decision relating to the operation of the company's bank accounts is a part of the managerial power of the directors. The mere fact that a director is not being associated with the operation of the company's bank accounts, does not constitute oppression or mismanagement. (*Sudha M. Singh vs. Eagle Cones Pvt. Ltd (2000) 36 CLA 189*)
4. The decision of the Board of Directors of the company to write-off bad debts is a commercial decision and does not require any judicial interference.
5. The members of the company, Minions Private Limited have filed an application for oppression in the company. To prove their facts, the members have requested for the inspection of documents of the company. However, the company denied to provide the same. Discuss, whether this amount to oppression under the provisions of this Act?

The right to inspection of documents and books of account of a company is not limited to the Board of directors. In order to prove allegations made in a petition under section 241 (erstwhile section of the Act), the shareholders are entitled to be allowed inspection of the books of account and other relevant papers of the company. However, mere denial of inspection, whether during the pendency of the petition or before it, does not amount to an act of oppression as held in the case of *Lalita Rajya Lakshmi v. Indian Motor Co. (Hazaribagh)*

Ltd. (1962) 32 Com Cases 207.

If a petitioner cannot make out a case of mismanagement and oppression because he was unable to collect materials for the purpose, it is not for the court to direct the directors of the company to offer inspection of the company's books and accounts so as to enable a petitioner to collect materials for the petition under the Act.

6. In deciding an application under section 241 and 242 (erstwhile section of the Act), a single act of renting out the premises of the company without the knowledge of the members cannot be termed as oppression or mismanagement. In other words, the act of oppression must be a continuing one.
7. The power to issue shares should be exercised bona-fide in the interest of the company and not for benefiting the directors or any other group. The directors are in a fiduciary position with the company and must exercise their power to issue the shares for the benefit of the company. If the power is exercised solely for their personal benefits, the Tribunal may interfere and prevent the directors from doing so. The act of issue of further shares by the directors of a company for the purpose of converting a majority into minority is a grave act of oppression.



5. CONSEQUENCES OF TERMINATION OR MODIFICATION OF CERTAIN AGREEMENTS [SECTION 243]

- (1) **Consequence of termination or modifications of certain agreements by an order passed by the Tribunal:** Where an order made under section 242 terminates, sets aside or modifies an agreement such as is referred to in sub-section (2) of that section,—
 - (a) **such order shall not give rise to any claims** whatever against the company by any person for damages or for compensation for loss of office or in any other respect either in pursuance of the agreement or otherwise;
 - (b) **no managing director or other director or manager** whose agreement is so terminated or set aside shall, **for a period of five years** from the date of the order terminating or setting aside the agreement, **without the leave of the Tribunal, be appointed, or act**, as the managing director or other director or manager of the company:
- (1A) **Disqualified to hold office:** The person who is **not a fit and proper** person pursuant to sub-section (4A) of section 242 shall **not hold the office of a director or any other office** connected with the conduct and management of the affairs of any company for a period of **five years** from the date of the said decision:

Provided that the Central Government may, with the leave of the Tribunal, permit such person to hold any such office before the expiry of the said period of five years.

- (1B) **No Compensation for loss / termination of office:** Notwithstanding anything contained in any other provisions of this Act, or any other law for the time being in force, or any contract, memorandum or articles, on the removal of a person from the office of a director or any other office connected with the conduct and management of the affairs of the company, that person shall **not be entitled to, or be paid, any compensation** for the loss or termination of office.

Provided that the **Tribunal shall not grant leave** under this clause unless **notice of the intention to apply for leave** has been served on the Central Government and that Government has been given a reasonable opportunity of being heard in the matter.

- (2) **Penalty:** Any person who knowingly acts as a managing director or other director or manager of a company in contravention of clause (b) of sub-section (1) or sub-section (1A), and every other director of the company who is knowingly a party to such contravention, shall be punishable with fine which may extend to five lakh rupees.



6. CLASS ACTION [SECTION 245]

Section 245 of the Companies Act, 2013 introduces the concept of class action by shareholders and depositors of a company with substantive remedies. According to this section, members and depositors, or an individual member or depositor, can file a petition for reliefs, if they are of the opinion that the affairs of the company are being managed or conducted in a manner prejudicial to the interests of the company, its members or depositors.



- (1) **Filing of application before the Tribunal on behalf of the members or depositors [Sub-section (1)]:**

Such number of **member or members, depositor or depositors or any class of them**, as the case may be, as are indicated in sub-section (3) may, if they are of the opinion that the management or conduct of the affairs of the company are being conducted in a manner **prejudicial to the interests of the company or its members or depositors**, file an application before the Tribunal on behalf of the members or depositors for seeking all or any of the following orders, namely:—

- to **restrain the company** from committing an **act** which is **ultra vires** the articles or memorandum of the company;
- to **restrain the company** from committing **breach of any provision** of the company's memorandum or articles;
- to **declare a resolution** altering the memorandum or articles of the company **as void** if the resolution was **passed by suppression of material facts or obtained by mis-statement** to the members or depositors;
- to **restrain** the company and its directors from **acting on such resolution**;

- (e) to **restrain** the company from **doing an act** which is **contrary to the provisions** of this Act or any other law for the time being in force;
- (f) to **restrain** the company from **taking action contrary to any resolution passed** by the members;
- (g) to **claim damages or compensation or demand any other suitable action** from or against—
 - (i) the company or its directors for any **fraudulent, unlawful or wrongful act or omission or conduct** or any likely act or omission or conduct on its or their part;
 - (ii) the auditor including audit firm of the company for any **improper or misleading statement of particulars made in his audit report** or for any fraudulent, unlawful or wrongful act or conduct; or
 - (iii) any expert or advisor or consultant or any other person for any **incorrect or misleading statement** made to the company or for any fraudulent, unlawful or wrongful act or conduct or any likely act or conduct on his part;
- (h) to **seek any other remedy** as the Tribunal may deem fit.

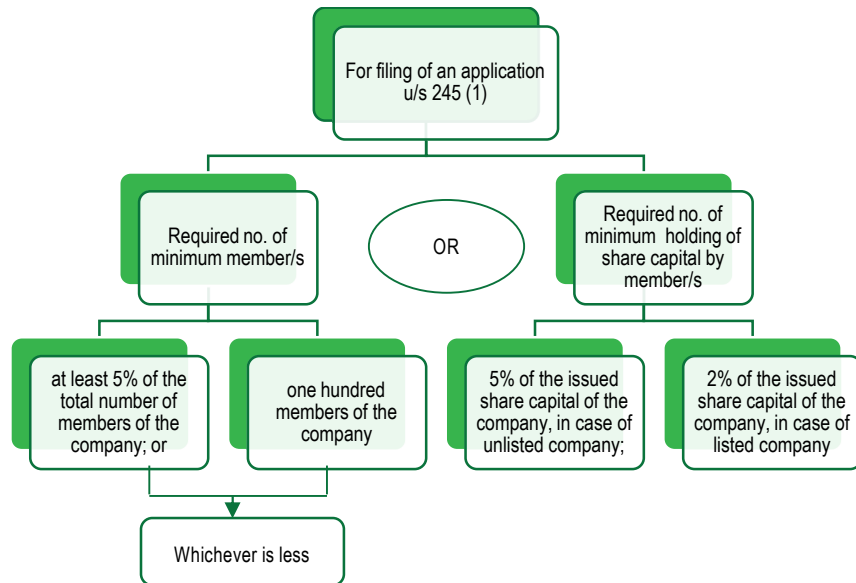
(2) Liability of Audit Firm and its Partners [Sub-section (2)]:

Where the **members or depositors** seek any damages or compensation or demand any other suitable action from or against an **audit firm**, the liability shall be of the **firm** as well as of **each partner** who was involved in making any improper or misleading statement of particulars in the audit report or who acted in a fraudulent, unlawful or wrongful manner.

(3) Requisite number of members to apply [Sub-section (3)]:

- (i) The **requisite number of members** provided in sub-section (1) shall be as under:—
 - (a) **in the case of a company having a share capital**, not less than **one hundred members** of the company or not less than such **percentage of the total number of its members** as may be prescribed, **whichever is less**, or any member or members holding not less than such **percentage of the issued share capital of the company** as may be prescribed, subject to the condition that the applicant or applicants has or have paid all calls and other sums due on his or their shares;

In case of a company having a share capital, the requisite number of member or members to file an application under section 245 (1) shall be as given hereunder –



- (b) in the case of a company not having a share capital, not less than **one-fifth** of the total number of its members.
- (ii) The requisite number of depositors provided in sub-section (1) shall not be less than **one hundred depositors** or not less than such **percentage of the total number of depositors** as may be prescribed, **whichever is less**, or any depositor or depositors to whom the company owes such percentage of total deposits of the company as may be prescribed.

The **requisite number of depositor or depositors to file an application** under sub-section (1) of section 245 shall be -

- (i) (a) at least five percent of the total number of depositors of the company; or
 (b) one hundred depositors of the company,
 whichever is less; or;
- (ii) depositor or depositors to whom the company owes five percent of total deposits of the company.

(4) Requirements for consideration of application [Sub-section (4)]:

In considering an application under sub-section (1), the Tribunal shall take into account, in particular—

- (a) whether the member or depositor is acting in **good faith** in making the application for seeking an order;
- (b) any evidence before it as to the **involvement** of any person other than directors or officers of the company on any of the matters provided in clauses (a) to (f) of sub-section(1);

- (c) whether the cause of action is one which the member or depositor could pursue in his **own right** rather than through an order under this section;
- (d) any evidence before it as to the **views** of the members or depositors of the company who **have no personal interest**, direct or indirect, in the matter being proceeded under this section;
- (e) where the cause of action is an act or omission that is **yet to occur**, whether the act or omission could be, and in the circumstances would be likely to be—
 - (i) authorised by the company before it occurs; or
 - (ii) ratified by the company after it occurs;
- (f) where the cause of action is an act or omission that has **already occurred**, whether the act or omission could be, and in the circumstances would be likely to be, ratified by the company.

(5) In case of admission of application [Sub-section (5)]:

If an application filed under sub-section (1) is admitted, then the Tribunal shall have regard to the following, namely:—

- (a) **public notice shall be served** on admission of the application to all the members or depositors of the class in such manner as may be prescribed;
- (b) all **similar applications** prevalent in any jurisdiction should be consolidated into a single application and the class members or depositors should be allowed to **choose the lead applicant** and in the event the members or depositors of the class are unable to come to a consensus, the Tribunal shall have the power to appoint a lead applicant, who shall be in charge of the proceedings from the applicant's side;
- (c) **two class action applications** for the **same cause of action** shall **not** be allowed;
- (d) the **cost or expenses** connected with the application for class action shall be **defrayed** by the company or any other person **responsible for any oppressive act**.

(6) Order of Tribunal to be binding [Sub-section (6)]:

Any order passed by the Tribunal shall be **binding** on the company and all its members, depositors and auditor including audit firm or expert or consultant or advisor or any other person associated with the company.

(7) Punishment for non-compliance [Sub-section (7)]:

Any **company** which fails to comply with an order passed by the Tribunal under this section shall be **punishable with fine** which shall be at least five lakhs rupees but which may extend to twenty-five lakhs rupees and **every officer of the company** who is in default shall be punishable with **imprisonment** for a term which may extend to three years and **with fine** which shall be at least twenty-five thousand rupees but which may extend to one lakh rupees.

In addition to this punishment, penalties given under sections 337 to 341 (both inclusive) shall also apply.

(8) Application filed is found to be frivolous/vexatious [Sub-section (8)]:

Where any application filed before the Tribunal is found to be frivolous or vexatious, it shall, for reasons to be recorded in writing, **reject the application** and make an **order** that the **applicant shall pay** to the opposite party such **cost**, not exceeding one lakh rupees, as may be specified in the order.

(9) Exemption to banking company [Sub-section (9)]:

Nothing contained in this section shall apply to a **banking company**.

(10) Application may be filed on behalf of affected persons [Sub-section (10)]:

Subject to the compliance of this section, an application may be filed or any other action may be taken under this section by any person, group of persons or any association of persons representing the persons affected by any act or omission, specified in sub-section (1).



7. APPLICATION OF CERTAIN PROVISIONS TO PROCEEDINGS UNDER SECTION 241 OR SECTION 245 [SECTION 246]

The provisions of sections 337, 338, 339, 340 and 341 related to winding up, shall apply *mutatis mutandis*, in relation to an application made to the Tribunal under section 241 or section 245.

- Penalty for Frauds by Officers [Section 337]
- Liability where Proper Accounts not Kept [Section 338]
- Liability for Fraudulent Conduct of Business [Section 339]
- Power of Tribunal to Assess Damages Against Delinquent Directors, etc. [Section 340]
- Liability Under Sections 339 and 340 to Extend to Partners or Directors in Firms or Companies [Section 341]

In other words:

- The section seeks to provide that the provisions of the section 337 to 341 relating to power to punish for contempt of Tribunal shall apply in relation to a fraudulent application made to the Tribunal for oppression and mismanagement.
- The provisions of section 337 to 341 deal with offences by officers, contributories and promoters of a company after its winding up and provide for penalties and recompense for falsification of books, frauds committed by officers, failure to keep proper accounts, fraudulent conduct of business, and the power to assess damages against such delinquent officers, including partners and directors where a firm or a body is involved.

TEST YOUR KNOWLEDGE

Multitple Choice Questions

1. *Due to the impending recession, the profits of Super Star Car Manufacturers Limited decreased considerably for the financial year 2020-2021 and therefore, its Board of Directors did not recommend any dividend for the year. At the Annual General Meeting of Super Star Car Manufacturers Limited, a group of shareholders objected to the Board's decision of not recommending any dividend and coerced the directors to reverse such decision. On refusal by the Board, the disappointed members felt oppressed and filed a complaint with the National Company Law Tribunal (NCLT) against the action of the Board. In the given scenario, which option out of the four mentioned below, is the most appropriate:*
 - (a) *The contention of the shareholders of Super Star Car Manufacturers Limited who filed a complaint with NCLT against the action of the Board for not recommending dividend shall be tenable.*
 - (b) *The action of the Board of Directors of Super Star Car Manufacturers Limited, not to recommend any dividend shall amount to oppression and mismanagement.*
 - (c) *The action of the Board of Directors of Super Star Car Manufacturers Limited who acted in the interest of the company by not recommending any dividend shall not amount to oppression and mismanagement.*
 - (d) *Both (a) and (b).*
2. *The shareholders of Viable Plastic Industries Limited passed a special resolution at the Extra-ordinary General (EGM) of the company to alter the Articles of Association and empower Board of Directors to transfer the shares of any shareholder who competes with the business of the company. Mr. Akshat, one of the minority shareholders of Viable Plastic Industries Limited who was carrying on a competing business of manufacturing plastic bottles and containers as well as marketing them, challenged the validity of the alteration to be made in the Articles of Association and claimed such action as oppression against minority. Which of the option from the following four is applicable in the given situation?*
 - (a) *The action of Mr. Akshat challenging the validity of the alteration to be made in the Articles of Association and claiming such action as oppression against minority is not valid since the Articles are being altered after following the due process of law.*
 - (b) *The action of Mr. Akshat challenging the validity of the alteration to be made in the Articles of Association and claiming such action as oppression against minority is not valid since the Articles are being altered in the interest of the company.*
 - (c) *The action of Mr. Akshat challenging the validity of the alteration to be made in the Articles of Association and claiming such action as oppression against minority is valid since the act complained of is oppressive and prejudicial to the interest of the company.*
 - (d) *Both (a) and (b)*

3. Meenu Automotive Private Limited, whose issued and paid-up share capital is ₹ 1,00,00,000 consisting of 1,00,000 lakh equity shares of ₹ 100 each, has 150 shareholders as per its Register of Members. Some of the shareholders are contemplating to file an application before the National Company Law Tribunal (NCLT) alleging various acts of fraud and mismanagement. Which of the following options correctly indicates as to who can apply to the National Company Law Tribunal (NCLT) for relief against oppression and mismanagement happening in a company having share capital:
- In the above case such shareholders who are contemplating to file an application before the National Company Law Tribunal (NCLT) alleging various acts of fraud and mismanagement must be minimum one hundred and twenty five or not less than one-fifth of the total number of members, whichever is more, or any member or members holding at least one-fifth of the issued share capital on which all the calls have been paid.
 - In the above case such shareholders who are contemplating to file an application before the National Company Law Tribunal (NCLT) alleging various acts of fraud and mismanagement must be minimum fifty or not less than one-tenth of the total number of members, whichever is more, or any member or members holding at least one-fifteenth of the issued share capital on which all the calls have been paid.
 - In the above case such shareholders who are contemplating to file an application before the National Company Law Tribunal (NCLT) alleging various acts of fraud and mismanagement must be minimum seventy five or not less than one-fifth of the total number of members, whichever is less, or any member or members holding at least one-twentieth of the issued share capital on which all the calls have been paid.
 - In the above case such shareholders who are contemplating to file an application before the National Company Law Tribunal (NCLT) alleging various acts of fraud and mismanagement must be minimum one hundred or not less than one-tenth of the total number of members, whichever is less, or any member or members holding at least one-tenth of the issued share capital on which all the calls have been paid.
4. The issued and paid-up equity share capital of Golden Kalash Clothes Private Limited is ₹ 1,00,00,000 (10,00,000 equity shares of ₹ 10 each) which is held by ten shareholders. Jasmine holds 80,000 equity shares worth ₹ 8,00,000. Sensing oppression and mismanagement in the company, she is contemplating to apply to the National Company Law Tribunal (NCLT) for relief. Out of the following four options which one is applicable in the given situation:
- Jasmine being a single member cannot apply for relief against oppression and mismanagement propagated by Golden Kalash Clothes Private Limited since at least 60% of total shareholders must apply for such relief i.e. at least 6 shareholders in the present case.
 - Jasmine cannot apply to the National Company Law Tribunal (NCLT) for relief against oppression and mismanagement since she is holding 80,000 equity shares worth ₹

8,00,000 which is less than one-tenth of the issued and paid-up equity share capital of Golden Kalash Clothes Private Limited.

- (c) Jasmine, being one-tenth of the total number of shareholders, can apply to the National Company Law Tribunal (NCLT) for relief against oppression and mismanagement propagated by Golden Kalash Clothes Private Limited.
 - (d) Jasmine, being a single member, cannot apply for relief against oppression and mismanagement propagated by Golden Kalash Clothes Private Limited since at least 50% of total shareholders must apply for such relief i.e. at least 5 shareholders in the present case.
5. For the past five years Mr. Rohtash was the holder 5,500 shares of Delta Software Solutions Ltd. which has issued share capital of ₹ 5,00,000 divided into 50,000 shares of ₹ 10 each. Mr. Rohtash was in the knowledge of some material changes that had taken place in Delta Software Solutions Ltd. and according to him they were prejudicial to the interest of members as well as the company. To contain the directors from continuing with unjustified changes, he wanted to make an application to the jurisdictional National Company Law Tribunal (NCLT) under Section 241 of the Companies Act, 2013. However, before Mr. Rohtash could proceed further and file the application with NCLT, he expired within one hour because of severe heart attack. Immediately thereafter, his only son Umang, a child specialist working in the Government Hospital, inherited his 5,500 shares. Is it possible for Umang to file an application with the jurisdictional National Company Law Tribunal (NCLT) highlighting the conduct of the affairs of the company in a manner which is prejudicial to the interest of members as well as the company. Choose the correct option from those given below whether Umang can proceed further:
- (a) Though Mr. Rohtash was eligible under Section 244 of the Companies Act, 2013 to make an application to the jurisdictional National Company Law Tribunal (NCLT) but his son Umang cannot file the application because he has not yet completed six months as holder of the shares which he inherited after the death of his father Mr. Rohtash.
 - (b) Though Mr. Rohtash was eligible under Section 244 of the Companies Act, 2013 to make an application to the jurisdictional National Company Law Tribunal (NCLT) but his son Umang cannot file the application because he has not yet completed four months as holder of the shares which he inherited after the death of his father Mr. Rohtash.
 - (c) Though Mr. Rohtash was eligible under Section 244 of the Companies Act, 2013 to make an application to the jurisdictional National Company Law Tribunal (NCLT) but his son Umang cannot file the application because he has not yet completed three months as holder of the shares which he inherited after the death of his father Mr. Rohtash.
 - (d) Since Mr. Rohtash was eligible under Section 244 of the Companies Act, 2013 to make an application to the jurisdictional National Company Law Tribunal (NCLT), his son Umang can also file the application because he has inherited the 5,500 shares after the death of his father Mr. Rohtash.

6. Mr. Derek Jonathan, a majority shareholder, represented himself to be the Managing Director of Floyd Ceramics Ltd., and also discharged the functions in the capacity as Managing Director. However, he was not formally appointed as Managing Director of Floyd Ceramics Ltd. A group of six members, holding 1/12th of the issued share capital, which amounted to 1/10th of paid-up share capital of the company filed an application with the National Company Law Tribunal (NCLT) claiming that such an act of Mr. Derek Jonathan constituted oppression. The total number of members of Floyd Ceramics Ltd. are seventy-two. Which of the following statements is the most appropriate one in the above-mentioned situation?
- The group of six members cannot file an application with National Company Law Tribunal (NCLT) as the strength of members is less than 1/10th of total number of members of Floyd Ceramics Ltd. However, after filing the application with NCLT, it is within the discretion of NCLT to allow the application to be filed even with fewer number of members.
 - The group of six members cannot file an application with National Company Law Tribunal (NCLT) since the members hold less than 1/10th of the issued share capital of the company.
 - The group of six members cannot file an application with the National Company Law Tribunal (NCLT) since the given fact pattern does not constitute oppression.
 - Since the group of six members holds 1/10th of the paid-up share capital of the company, they can file an application with the National Company Law Tribunal (NCLT).

Descriptive Questions

- ABC Private Limited having share capital has eight shareholders. Can a member holding less than one-tenth of the share capital of the company apply to the Tribunal for relief against oppression and mismanagement? Give your answer according to the provisions of the Companies Act, 2013.
- The issued and paid up capital of MNC Limited is ₹ 5 crores consisting of 5,00,000 equity shares of ₹ 100 each. The said company has 500 members. A petition was submitted before the Tribunal signed by 80 members holding 10,000 equity shares of the company for the purpose of relief against oppression and mismanagement by the majority shareholders. Examining the provisions of the Companies Act, 2013, decide whether the said petition is maintainable. Also explain the impact on the maintainability of the above petition, if subsequently 40 members, who had signed the petition, withdrew their consent.
- A group of shareholders consisting of 25 members decide to file a petition before the Tribunal for relief against oppression and mismanagement by the Board of Directors of Fly By Night Operators Ltd. The company has a total of 300 members and the group of 25 members holds one-tenth of the total paid-up share capital accounting for one-fifteenth of the issued share capital. The main grievance of the group is that due to mismanagement by the Board of Directors, the company is incurring losses and the company has not declared any dividends even when profits were available in the past years for declaration of dividend. In the light of

the provisions of the Companies Act, 2013, advise the group of shareholders regarding the success of (i) getting the petition admitted and (ii) obtaining relief from the Tribunal.

4. A group of members of XYZ Limited has filed a petition before the Tribunal alleging various acts of oppression and mismanagement by the majority shareholders of the company. The Petitioner group holds 12% of the issued share capital of the company. During the pendency of the petition, some of the petitioners holding about 5% of the issued share capital of the company wish to disassociate themselves from the petition and they along with the other majority shareholders have submitted before the Tribunal that the petition may be dismissed on the ground of non-maintainability. Examine their contention having regard to the provisions of the Companies Act, 2013.
5. A group of members holding 380 lakh issued share capital in Zolo Tech Ltd. a listed public company having total issued share capital of 15000 lakhs as per latest financial statements alleged that company Board of Directors is conducting an act which is ultra vires the Articles or Memorandum of the company without altering the Memorandum or Articles of the company. They make an application to Tribunal (NCLT) to restrain the company from doing such ultra-vires act. With reference to the provision of Companies Act, 2013 ascertain whether the application will be admitted by tribunal (NCLT).

ANSWERS

Answer to Multiple Choice Questions

1.	c	2.	d	3.	d	4.	c	5.	d
6.	c								

Answer to Descriptive Questions

1. According to Section 244 of the Companies Act, 2013, in the case of a company having share capital, the following member(s) have the right to apply to the Tribunal under section 241:
 - (a) Not less than 100 members of the company or not less than one-tenth of the total number of members, whichever is less; or
 - (b) Any member or members holding not less than one-tenth of the issued share capital of the company provided the applicant(s) have paid all the calls and other sums due on the shares.

In the given case, there are eight shareholders in ABC Private Limited. As per the condition (a) above, 10% of 8 i.e. 1 member can apply to the Tribunal. Therefore, a single member can present a petition to the Tribunal, regardless of the fact that he holds less than one-tenth of the company's share capital.

2. As per the provisions of Section 244 of the Companies Act, 2013, in the case of a company having share capital, members eligible to apply for oppression and mismanagement shall be lower of the following:

100 members; or

1/10th of the total number of members; or

Members holding not less than 1/10th of the issued share capital of the company.

The share holding pattern of MNC Limited is as follows:

₹ 5,00,00,000 equity share capital held by 500 members

The petition alleging oppression and mismanagement has been made by some members as follows:

(i) No. of members making the petition – 80

(ii) Amount of share capital held by members making the petition – ₹ 10,00,000

The petition shall be valid if it has been made by the lowest of the following:

100 members; or

50 members (being 1/10th of 500); or

Members holding ₹ 50,00,000 share capital (being 1/10th of ₹ 5,00,00,000)

As it is evident, the petition made by 80 members meets the eligibility criteria specified under section 244 of the Companies Act, 2013 as it exceeds the minimum requirement of 50 members in this case. Therefore, the petition is maintainable.

The consent to be given by a shareholder is reckoned at the beginning of the proceedings. The withdrawal of consent by any shareholder during the course of proceedings shall not affect the maintainability of the petition [*Rajamundhry Electric Corporation Vs. V. Nageswar Rao A.I.R.*].

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

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

(ii) In the case of company not having share capital, not less than one-fifth of the total number of its members.

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

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

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

Similarly, failure to declare dividends or payment of low dividends also does not amount to oppression. (*Thomas Veddon V.J. vs. Kuttanad Robber Co. Ltd*).

Thus, the shareholders may not succeed in getting any relief from Tribunal.

4. The argument of the majority shareholders that the petition may be dismissed on the ground of non-maintability is not correct. The proceedings shall continue irrespective of withdrawal of consent by some petitioners. It has been held by the Supreme Court in *Rajmundhry Electric Corporation vs. V. Nageswar Rao*, AIR (1956) SC 213 that if some of the consenting members have subsequent to the presentation of the petition withdraw their consent, it would not affect the right of the applicant to proceed with the petition. Thus, the validity of the petition must be judged on the facts as they were at the time of presentation. Neither the right of the applicants to proceed with the petition nor the jurisdiction of Tribunal to dispose it of on its merits can be affected by events happening subsequent to the presentation of the petition.
5. According to section 245 of Companies Act, 2013, such number of member or members, depositor or depositors or any class of them, as the case may be, as are indicated in sub-section (2) may, if they are of the opinion that the management or conduct of the affairs of the company are being conducted in a manner prejudicial to the interests of the company or its members or depositors, file an application before the Tribunal on behalf of the members or depositors for seeking an order, to restrain the company from committing an act which is ultra-vires the Articles or Memorandum of the company.

Requisite number of members to make Application under Section 245 (1) for Class Action for depositors is as prescribed in Rule 84 (4) of the National Company Law Tribunal Rules, 2016. Accordingly, in case of a company having a share capital the requisite number of member or members to file an application under section 245 (1) shall be:-

- (a) at least five per cent. of the total number of members of the company; or
- (b) one hundred members of the company, whichever is less; or
- (c) In case of a listed company, member or members holding not less than two per cent. of the issued share capital of the company.

In the above case, members holding 2.53% ($380/15000 \times 100$) of issued share capital of Zolo Tech Ltd. which is a listed company make an application before Tribunal (NCLT). Hence as members meet condition of 2% of issued share capital, therefore their application can be admitted by the NCLT.

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CHAPTER

7

WINDING UP



LEARNING OUTCOMES

After end of this Chapter, you will be able to:

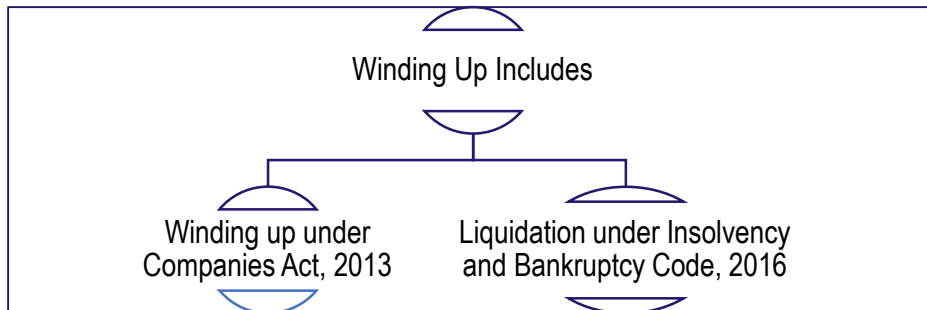
- ☐ Elucidate winding up process and its modes
- ☐ Brief on winding up of a company by the Tribunal
- ☐ Know the Persons who can make Petition for winding up
- ☐ List the Powers of Tribunal
- ☐ Explain the appointment of Company Liquidator
- ☐ Comprehend the procedure for winding up to be monitored by the Tribunal
- ☐ Know about the settlement of list of contributories and application of assets
- ☐ Explain the constitution of Advisory Committee
- ☐ List the powers and duties of Company Liquidator



1. INTRODUCTION

Companies Act, 2013 contains provisions relating to winding up of companies. However, Insolvency and Bankruptcy Code, 2016 which was enforced in 2016, has made substantial changes in these provisions. Provisions for application for winding up for “Inability to pay debts” has been omitted.

As per Section 2 (94A) of the Companies Act, 2013, the term “winding up” means winding up under this Act or liquidation under the Insolvency and Bankruptcy Code, 2016, as applicable.



2. MODES OF WINDING UP [SECTION 270]

The provisions of Part I of the Chapter XX of the Companies Act, 2013 shall apply to the winding up of a company by the Tribunal under this Act.

PART I: WINDING UP BY THE TRIBUNAL [SECTION 271 – 303]

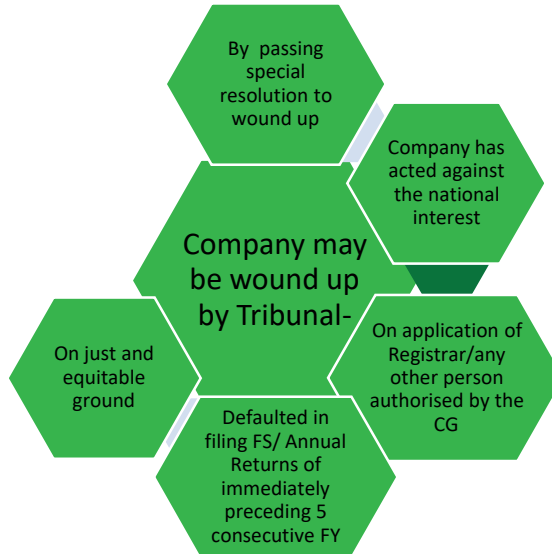


3. CIRCUMSTANCES IN WHICH COMPANY MAY BE WOUND UP BY TRIBUNAL [SECTION 271]

A company may, on a petition under section 272, be wound up by the Tribunal—

- if the company has, **by special resolution**, resolved that the company be wound up by the Tribunal;
- if the company has acted **against the interests** of the sovereignty and integrity of India, the security of the State, friendly relations with foreign States, public order, decency or morality;
- if **on an application** made by the Registrar or any other person authorised by the Central Government by notification under this Act, the Tribunal is of the opinion that the affairs of the company have been conducted in a fraudulent manner or the company was formed for fraudulent and unlawful purpose or the persons concerned in the formation or management of its affairs have been guilty of fraud, misfeasance or misconduct in connection therewith and that it is proper that the company be wound up;

- (d) if the company has made a **default in filing** with the Registrar its financial statements or annual returns for immediately preceding five consecutive financial years; or
- (e) if the Tribunal is of the opinion that it is **just and equitable** that the company should be wound up.



1. The Supreme Court of India in *Spicejet Ltd. v. Credit Suisse AG*, January 28, 2022 decided that High Court's order upholding admission of winding up petition against Spice Jet was to be stayed.

As per the facts, Appellant 'Spice Jet' was indebted to respondent (a global investment bank and financial services firm) for more than USD 24 million, non-payment of which had led to filing of and admission of winding up petition as ordered by single Judge. Appellant raised a defence that documents relied by respondent were not stamped and therefore, Courts in India would not take cognizance thereof. High Court by impugned order upheld admission of winding up petition on ground that such a defence could not be said to be a bona fide defence and at stage of admission of petition, it need not be gone into. It was decided by the Honourable Supreme Court that impugned order passed by High Court was to be stayed and appellant was to be granted three weeks' time to resolve its dispute with respondent.

2. The Supreme Court of India in *IDBI Bank Ltd. v. Official Liquidator* held that transfer or any other act done in relation to property of a company within a period of six months before commencement of its winding up shall be deemed to be a fraudulent preference of its creditors and accordingly be invalid.

3. The High Court of Karnataka in *Vardhman Yarns and Threads Ltd. v. Indus Garments (India) (P.) Ltd.* passed an order that where in e-mail respondent-company had acknowledged to pay outstanding dues to petitioner-company but had failed to pay same and respondent also admitted that its business operation had been stopped, it was just and equitable that respondent company be wound up.

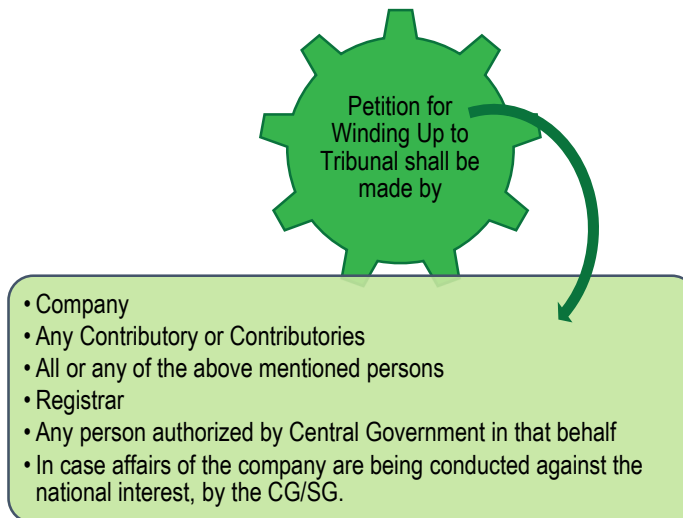
In the said case, Petitioner company filed winding up petition against respondent-company for its failure to pay outstanding dues in respect of supply of threads and other materials. In the said case it was held

that since in e-mail respondent company had acknowledged to pay outstanding dues to petitioner company but had failed to pay same and also it was admitted that business operation of respondent company had been stopped, it was just and equitable ground on the basis of which the respondent company may be wound up.



4. PETITION FOR WINDING UP [SECTION 272]

- (1) **Persons who can present Petition for winding up:** Subject to the provisions of this section, petition before Tribunal may be presented by the following:
- the company;
 - any contributory or contributories;
 - all or any of the persons specified in clauses (a) and (b);
 - the Registrar;
 - any person authorised by the Central Government in that behalf;
 - in a case falling under clause (b) of Section 271, by the Central Government or a State Government.



- (2) **Petition by contributory:** A contributory shall be entitled to present a petition for the winding up of a company.

Shares in respect of which he is a contributory or some of them were either originally allotted to him or have been held by him, and registered in his name, for at least six months during the eighteen months immediately before the commencement of the winding up or have devolved on him through the death of a former holder.

Contributory can file petition, though-

- He may be the holder of fully paid-up shares.
- The company may have no assets at all.
- The company may have no surplus assets left for distribution among the shareholders after the satisfaction of its liabilities.

- (3) **Petition by Registrar:** The Registrar shall be entitled to present a petition for winding up under section 271, except on the grounds specified in clause (a) of that section.

Provided that the Registrar shall obtain the previous sanction of the Central Government to the presentation of a petition:

Provided further that the Central Government shall not accord its sanction unless the company has been given a reasonable opportunity of making representations.

- (4) **Petition presented by company:** A petition presented by the company for winding up before the Tribunal shall be admitted only if accompanied by a statement of affairs in such form and in such manner as may be prescribed.
- (5) **Copy of petition to be filed with Registrar:** A copy of the petition made under this section shall also be filed with the Registrar and the Registrar shall, without prejudice to any other provisions, submit his views to the Tribunal within 60 days of receipt of such petition.

The National Company Law Tribunal, Bengaluru Bench in *Union of India v. Megacity (Bangalore) Developers & Builders Ltd.* held that pursuant to investigation by SFIO into affairs of respondent company, NCLT suspended its existing board of directors and directed Central Government to appoint nominee directors, but, nominee directors were unable to run affairs of respondent company, thus, they filed an application to wind up respondent company, since, passing of winding up order is civil death of company, in order to protect interest of shareholders of company, one more opportunity was to be given to respondent company to set things right in affairs of company.

As per the facts laid down, Petitioner-Central Government directed Serious Fraud Investigation Officer (SFIO) to investigate in to affairs of respondent-real Estate Company. SFIO conducted investigation and submitted its report by pointing out various inconsistencies, frauds, illegality and stated that affairs of respondent were conducted adverse to interest of its creditors, investors, and consumers and against public interest. NCLT suspended existing Board of Directors of respondent as pleaded by SFIO and directed Central Government to appoint nominee directors. Central Government appointed three nominee directors. These appointed Nominee directors were unable to run affairs of respondent and expressed their difficulties to defend or prosecute cases filed by and against respondent. They thus, filed an application to wind up respondent real estate company. It was noted that passing of winding up order is civil death for company and, therefore, in order to protect interest of stakeholders of company, Courts/Tribunals, before passing such order, have to examine all issues concerning matter so as to see whether passing winding up order is only alternative or is there any possibility for revival of affairs of company. It was passed an order that one more opportunity was to be given to respondent to set things right in affairs of respondent . It

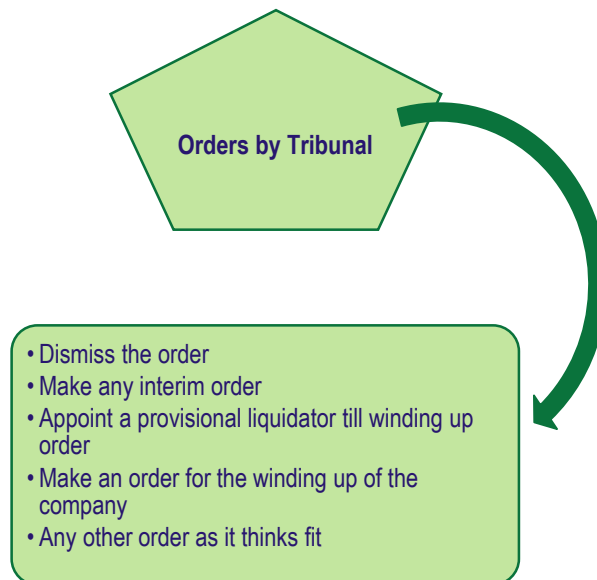
would, therefore, be just and proper to direct nominee directors to convene Extraordinary General Meeting (EGM) of shareholders of respondent so as to elect their proposed directors so that they could take all necessary actions to resolve all disputes, which lead to suspension of Board of Directors of respondent.



5. POWERS OF TRIBUNAL [SECTION 273]

(1) **Order passed by Tribunal:** The Tribunal may, on receipt of a petition for winding up under section 272 pass any of the following orders, namely:—

- (a) dismiss it, with or without costs;
- (b) make any interim order as it thinks fit;
- (c) appoint a provisional liquidator of the company till the making of a winding up order;
- (d) make an order for the winding up of the company with or without costs; or
- (e) any other order as it thinks fit:



Time limit for passing an order: An order under this sub-section shall be made within **ninety days** from the date of presentation of the petition.

Notice to company on appointing of provisional liquidator: Before appointing a provisional liquidator under clause (c) [given above], the Tribunal shall give notice to the company and afford a reasonable opportunity to it to make its representations, if any, unless for special reasons to be recorded in writing, the Tribunal thinks fit to dispense with such notice.

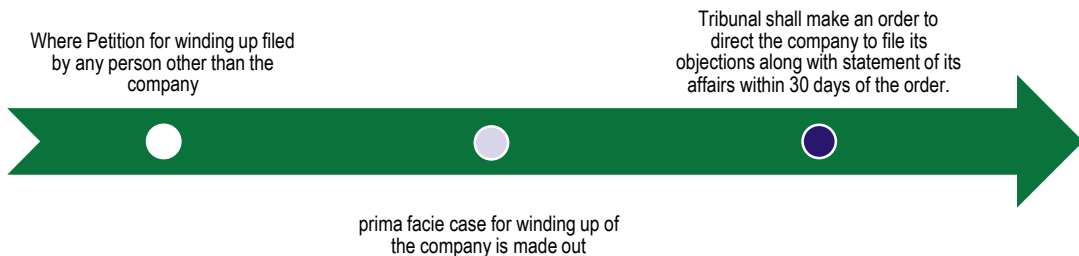
Tribunal not to refuse to make a winding up order: The Tribunal shall not refuse to make a winding up order on the ground only that the assets of the company have been mortgaged for an amount equal to or in excess of those assets, or that the company has no assets.

- (2) **Tribunal make order for any other remedy on just and equitable ground:** Where a petition is presented on the ground that it is just and equitable that the company should be wound up, the Tribunal may refuse to make an order of winding up, if it is of the opinion that some other remedy is available to the petitioners and that they are acting unreasonably in seeking to have the company wound up instead of pursuing the other remedy.



6. DIRECTIONS FOR FILING STATEMENT OF AFFAIRS [SECTION 274]

- (1) **Tribunal may order company to file a statement of its affairs:** Where a petition for winding up is filed before the Tribunal by any person other than the company, the Tribunal shall, if satisfied that a prima facie case for winding up of the company is made out, by an order direct the company to file its **objections along with a statement of its affairs** within thirty days of the order in such form and in such manner as may be prescribed.



Extension of time for filing: The Tribunal may allow a further period of **thirty days** in a situation of contingency or special circumstances.

Deposit of security: The Tribunal may direct the petitioner to deposit such security for costs as it may consider reasonable as a pre-condition to issue directions to the company.

- (2) **Punishment for not filing of the statement of affairs:** A company, which fails to file the statement of affairs as referred to in sub-section (1), shall forfeit the right to oppose the petition and such directors and officers of the company as found responsible for such non-compliance, shall be liable for punishment under sub-section (4).
- (3) **Directors and other officers to submit books of account completed and audited to the Liquidator:** The directors and other officers of the company, in respect of which an order for winding up is passed by the Tribunal under clause (d) of sub-section (1) of section 273, shall, within a period of **thirty days** of such order, submit, at the cost of the company, the books of

account of the company completed and audited up to the date of the order, to such liquidator and in the manner specified by the Tribunal.

- (4) **Penalty for Contravention:** If any director or officer of the company contravenes the provisions of this section, the director or the officer of the company who is in default shall be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than ₹ twenty-five thousand but which may extend to ₹ five lakh, or with both.
- (5) **Who may file Complaint before Special Court:** The complaint may be filed in this behalf before the Special Court by Registrar, provisional liquidator, Company Liquidator or any person authorised by the Tribunal.



7. COMPANY LIQUIDATORS AND THEIR APPOINTMENTS [SECTION 275]

- (1) **Appointment of official liquidator:** For the purposes of winding up of a company by the Tribunal, the Tribunal at the time of the passing of the order of winding up, shall appoint an Official Liquidator or a liquidator from the **panel maintained** (i.e. under the Insolvency Professional registered under Insolvency and Bankruptcy Code, 2016) as the Company Liquidator.
- (2) **Appointment of Provisional Liquidator or the Company Liquidator by Tribunal:** The provisional liquidator or the Company Liquidator, as the case may, shall be appointed by the **Tribunal from amongst the insolvency professionals** registered under the Insolvency and Bankruptcy Code, 2016.
- (3) **Tribunal may restrict the powers of a Provisional Liquidator:** Where a provisional liquidator is appointed by the Tribunal, the Tribunal may **limit and restrict his powers by the order appointing him or it or by a subsequent order**, but otherwise he shall have the same powers as a liquidator.
- (4) **Tribunal to specify the terms and conditions of appointment of Provisional Liquidator:** The terms and conditions of appointment of a provisional liquidator or Company Liquidator and the fee payable to him or it shall be **specified by the Tribunal** on the basis of task required to be performed, experience, qualification of such liquidator and size of the company.
- (5) **Filing of Declaration by Liquidator on Appointment:** On appointment as provisional liquidator or Company Liquidator, as the case may be, such liquidator shall **file a declaration** within **seven days** from the date of appointment in the prescribed form disclosing conflict of interest or lack of independence in respect of his appointment, if any, with the Tribunal and such obligation shall continue throughout the term of his appointment.

- (6) **Appointment of Provisional Liquidator as the Company Liquidator:** While passing a winding up order, the Tribunal may **appoint a provisional liquidator**, if any, appointed under clause (c) of sub-section (1) of section 273, **as the Company Liquidator** for the conduct of the proceedings for the winding up of the company.



8. REMOVAL AND REPLACEMENT OF LIQUIDATOR [SECTION 276]

- (1) **Removal of Provisional Liquidator or the Company Liquidator:** The Tribunal may, on a reasonable cause being shown and for reasons to be recorded in writing, remove the provisional liquidator (PL) or the Company Liquidator (CL), as the case may be, as liquidator of the company on any of the following **grounds**, namely:—
- misconduct;
 - fraud or misfeasance;
 - professional incompetence or failure to exercise due care and diligence in performance of the powers and functions;
 - inability to act as provisional liquidator or as the case may be, Company Liquidator;
 - conflict of interest or lack of independence during the term of his appointment that would justify removal.

Grounds for removal of PL/CL

misconduct;	fraud / misfeasance;	professional incompetence / failure to exercise due care and diligence	inability to act as provisional liquidator / Company Liquidator;	conflict of interest / lack of independence during the term of his appointment

- (2) **Transfer of work of Liquidator:** In the event of **death, resignation or removal** of the provisional liquidator or as the case may be, Company Liquidator, the Tribunal may transfer the work assigned to him or it to another Company Liquidator for reasons to be recorded in writing.
- (3) **Recovery of loss or damage from Liquidator:** Where the Tribunal is of the opinion that any liquidator is responsible for causing any **loss or damage** to the company due to **fraud or**

misfeasance or failure to exercise due care and diligence in the performance of his or its powers and functions, the Tribunal may recover or cause to be recovered such loss or damage from the liquidator and pass such other orders as it may think fit.

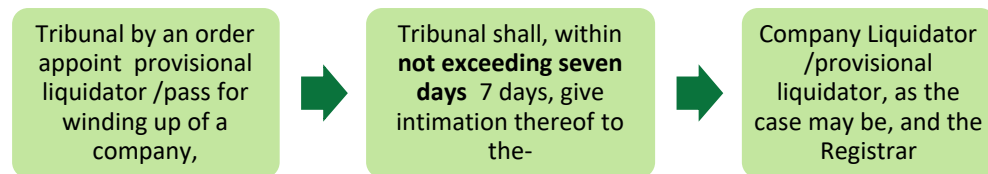
- (4) **Reasonable opportunity of being heard to be given the Provisional Liquidator:** The Tribunal shall, before passing any order under this section, provide a reasonable opportunity of being heard to the provisional liquidator or, as the case may be, Company Liquidator.



9. INTIMATION TO COMPANY LIQUIDATOR, PROVISIONAL LIQUIDATOR AND REGISTRAR [SECTION 277]

- (1) **Tribunal to cause intimation of its order:**

Where the Tribunal makes an order for appointment of provisional liquidator or for the winding up of a company, it shall, within a period **not exceeding seven days** from the date of passing of the order, cause intimation thereof to be sent to the Company Liquidator or provisional liquidator, as the case may be, and the Registrar.



- (2) **Registrar to notify the order of Tribunal in Official Gazette:**

With respect to all companies - On receipt of the copy of order of appointment of provisional liquidator or winding up order, the **Registrar** shall make an endorsement to that effect in his records relating to the company and **notify in the Official Gazette** that such an order has been made, and

In the case of a listed company, the Registrar shall intimate about such appointment or order, as the case may be, **to the stock exchange or exchanges** where the securities of the company are listed.

On receipt of order of Appointment of PL/CL or winding up, Registrar shall

in case of Listed Company

in case of all Companies

Intimate the stock exchange/s where the securities of the company are listed.

Make an endorsement to that effect in his records and notify in the Official Gazette

- (3) **Winding up order to be deemed to be notice of discharge:** The winding up order shall be deemed to be a **notice of discharge to the officers, employees and workmen** of the company, except when the business of the company is continued.
- (4) **Constitution of winding up committee to monitor liquidation proceedings:** Within **3 weeks** from the date of passing of winding up order, the Company Liquidator shall make an application to the Tribunal for constitution of a **winding up committee to assist and monitor the progress of liquidation proceedings by the Company Liquidator** in carrying out the function as provided in sub-section (5) and such winding up committee shall comprise of the following persons, namely:—
 - (i) Official Liquidator attached to the Tribunal;
 - (ii) nominee of secured creditors; and
 - (iii) a professional nominated by the Tribunal.
- (5) **Areas in which winding up committee to assist and monitor liquidation functions:** The **Company Liquidator** shall be the **convener** of the meetings of the **winding up committee** which shall **assist and monitor the liquidation proceedings** in following areas of liquidation functions, namely:—
 - (i) taking over assets;
 - (ii) examination of the statement of affairs;
 - (iii) recovery of property, cash or any other assets of the company including benefits derived there from;
 - (iv) review of audit reports and accounts of the company;
 - (v) sale of assets;
 - (vi) finalisation of list of creditors and contributories;
 - (vii) compromise, abandonment and settlement of claims;

- (viii) payment of dividends, if any; and
- (ix) any other function, as the Tribunal may direct from time to time.

Winding up
Committee –
For assistance
and monitoring
of Liquidation

taking over assets;

examination

recovery of property

review of audit reports and accounts

sale of assets

finalisation of list of creditors & contributories;

compromise, abandonment and settlements

payment of dividends

any other function, as directed by Tribunal

- (6) **Submission of report and minutes of meetings of the committee before Tribunal on monthly basis:** The Company Liquidator shall place before the Tribunal a **report along with minutes of the meetings of the committee on monthly basis** duly signed by the members present in the meeting for consideration till the final report for dissolution of the company is submitted before the Tribunal.
- (7) **Company liquidator to prepare draft final report:** The Company Liquidator shall prepare the **draft final report** for consideration and **approval of the winding up committee**.
- (8) **Submission of approved final report before the Tribunal for passing of dissolution order:** The final report so approved by the winding up committee shall be **submitted** by the Company Liquidator **before the Tribunal** for passing of a dissolution order in respect of the company.



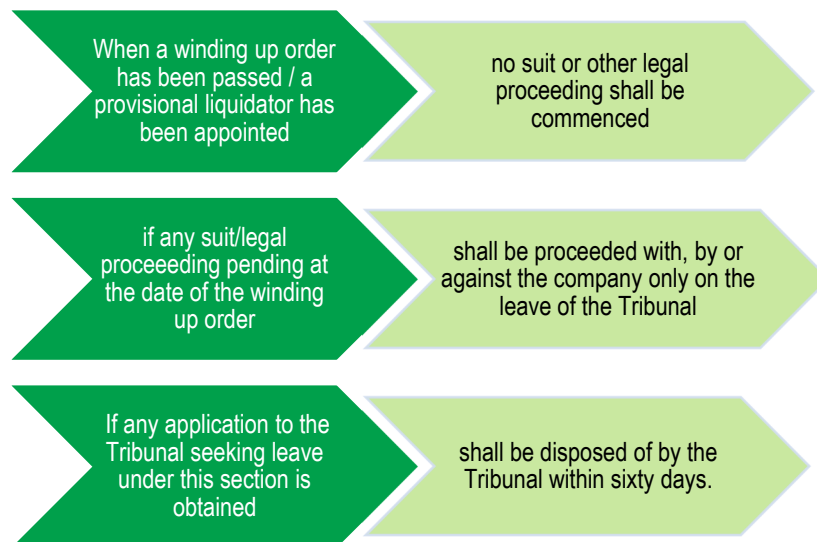
10. EFFECT OF WINDING UP ORDER [SECTION 278]

The order for the winding up of a company shall operate in favour of all the creditors and all contributories of the company as if it had been made out on the joint petition of creditors and contributories.



11. STAY OF SUITS, ETC. ON WINDING UP ORDER [SECTION 279]

- (1) Suit or legal proceeding can be commenced after winding up order/appointment of liquidator only with permission of Tribunal:



- (2) **What happens to proceeding pending in appeal before Supreme Court or a High Court:**
Nothing in sub-section (1) shall apply to any proceeding pending in appeal before the Supreme Court or a High Court.

Example 1: A provisional liquidator is appointed by the Tribunal for initiating the winding up process against TRS Ltd. An appeal against TRS Ltd. is pending before the High Court of Delhi on the date of appointment of the provisional liquidator. The management is of the opinion that since the provisional liquidator is appointed by the Tribunal, all the pending suits and actions can be proceeded with only after the permission of the Tribunal. The contention of TRS Ltd. does not hold good, in the light of section 279 (2). Accordingly, permission of Tribunal is not required in case of an appeal pending before High Court of Delhi.



12. JURISDICTION OF TRIBUNAL [SECTION 280]

The Tribunal shall have jurisdiction to **entertain**, or **dispose of**,—

- (a) any **suit or proceeding** by or against the company;
- (b) any **claim** made by or against the company, including claims by or against any of its branches in India;
- (c) any **application** made under section 233 [Fast track merger];
- (d) any **question of priorities** or any other question whatsoever, whether of **law or facts**, including those relating to assets, business, actions, rights, entitlements, privileges, benefits, duties, responsibilities, obligations or in any matter arising out of, or in relation to winding up of the company,

whether such suit or proceeding has been instituted, or is instituted, or such claim or question has arisen or arises or such application has been made or is made or such scheme has been submitted, or is submitted, before or after the order for the winding up of the company is made.



13. SUBMISSION OF REPORT BY COMPANY LIQUIDATOR [SECTION 281]

- (1) **Particulars to be mentioned in the Report of Company Liquidator:** Where the Tribunal has made a winding up order or appointed a Company Liquidator, such liquidator shall, within **sixty days from the order**, submit to the Tribunal, a **report** containing the following particulars, namely:—

Contents of Liquidator's Report

- The **nature and details of the assets of the company** including their location and value, stating separately the cash balance in hand and in the bank, if any, and the negotiable securities, if any, held by the company. The valuation of the assets shall be obtained from registered valuers for this purpose.
- **Amount of capital issued, subscribed and paid-up**
- The **existing and contingent liabilities** of the company including names, addresses and occupations of its creditors, stating separately the amount of secured and unsecured debts, and in the case of secured debts, particulars of the securities given, whether by the company or an officer thereof, their value and the dates on which they were given.
- The **debts due to the company** and the names, addresses and occupations of the persons from whom they are due and the amount likely to be realised on account thereof.

- **Guarantees**, if any, extended by the company
- **List of contributories and dues**, if any, payable by them and details of any unpaid call
- **Details of trademarks and intellectual properties**, if any, owned by the company
- **Details of subsisting contracts, joint ventures and collaborations**, if any
- **Details of holding and subsidiary companies**, if any
- **Details of legal cases** filed by or against the company
- **Any other information** which the Tribunal may direct or the Company Liquidator may consider necessary to include.

- (2) **Company Liquidator to include in his Report manner of formation of company and commission of any fraud in formation, etc.:** The Company Liquidator shall include in his report the manner in which the company was **promoted or formed** and whether in his opinion any fraud has been committed by any person in its promotion or formation or by any officer of the company in relation to the company since the formation thereof and **any other matters** which, in his opinion, it is desirable **to bring to the notice of the Tribunal**.
- (3) **Report on viability of business of the company:** The Company Liquidator shall also make a report on the viability of the business of the company or the steps which, in his opinion, are necessary for maximizing the value of the assets of the company.
- (4) **Permission to make additional reports:** The Company Liquidator may also, if he thinks fit, make any **further report or reports**.
- (5) **Inspection of report by a creditor or contributory:** Any person describing himself in writing to be a creditor or a contributory of the company shall be **entitled by himself or by his agent** at all reasonable times to **inspect the report** submitted in accordance with this section and **take copies** thereof or extracts therefrom on **payment** of the prescribed fees.



14. DIRECTIONS OF TRIBUNAL ON REPORT OF COMPANY LIQUIDATOR [SECTION 282]

- (1) **Fixation of Time limit for completion of proceedings and dissolution:** The **Tribunal** shall, on consideration of the report of the Company Liquidator, **fix a time limit** within which the entire proceedings shall be completed and the company be dissolved.

Revision of time limit: The Tribunal may, if it is of the opinion, at any stage of the proceedings, or on examination of the reports submitted to it by the Company Liquidator and after hearing the Company Liquidator, creditors or contributories or any other interested person, that it will not be advantageous or economical to continue the proceedings, **revise**

the time limit within which the entire proceedings shall be completed and the company be dissolved.

- (2) **Order of Tribunal:** The Tribunal may, on examination of the reports submitted to it by the Company Liquidator and after hearing the Company Liquidator, creditors or contributories or any other interested person, **order sale of the company as a going concern or its assets** or part thereof.

The Tribunal may, where it considers fit, **appoint a sale committee** comprising such creditors, promoters and officers of the company as the Tribunal may decide to assist the Company Liquidator in sale under this sub-section.

- (3) **Tribunal may order for investigation against the company in respect of commission of fraud:** Where a **report is received** from the Company Liquidator or the Central Government or any person that a **fraud has been committed** in respect of the company, the Tribunal shall, without prejudice to the process of winding up, **order for investigation** under section 210, and on consideration of the report of such investigation it may pass order and give directions under sections 339 to 342 or direct the Company Liquidator to file a criminal complaint against persons who were involved in the commission of fraud.
- (4) **Tribunal to take measures to safeguard the assets of the company:** The Tribunal may order for taking such steps and measures, as may be necessary, to protect, preserve or enhance the value of the assets of the company.
- (5) **Tribunal may pass such other order / directions as it may consider fit:** The Tribunal may pass such other order or give such other directions as it considers fit.



15. CUSTODY OF COMPANY'S PROPERTIES [SECTION 283]

S. No.	Provision	It states that-
1.	Where a winding up order has been made or where a provisional liquidator has been appointed-	The company liquidator or provisional liquidator, shall, on the order of the Tribunal immediately take into his or its custody or control – • all the property, • effects and • actionable claims to which the company is or appears to be entitled to and take such steps and measures, as may be necessary, to protect and preserve the properties of the company.

2.	Custody of Tribunal to be deemed from the date of winding up order	All the property and effects of the company shall be deemed to be in the custody of the Tribunal from the date of the order for the winding up of the company.
3.	On an application by the Company Liquidator, the Tribunal may order to pay / deliver etc. any money, property etc. of the company to the Liquidator.	The Tribunal may, at any time after the making of a winding up order, require any contributory for the time being on the list of contributories, and any trustee, receiver, banker, agent, officer or other employee of the company,- • to pay, • deliver, • surrender or • transfer forthwith, or • within such time as the Tribunal directs, • to the Company Liquidator, • any money, property or books and papers in his custody or under his control to which the company is or appears to be entitled.



16. PROMOTERS, DIRECTORS, ETC., TO COOPERATE WITH COMPANY LIQUIDATOR [SECTION 284]

- (1) **Various persons to extend full cooperation to the liquidators:** The promoters, directors, officers and employees, who are or have been in employment of the company or acting or associated with the company **shall extend full cooperation to the Company Liquidator** in discharge of his functions and duties.
- (2) **If a person does not cooperate, Company Liquidator may make application to Tribunal:** If any person required to assist or cooperate with the Company Liquidator **does not assist or cooperate**, the Company Liquidator may make an application to the Tribunal for necessary directions.
- (3) **Tribunal to direct non-cooperating person to comply with instructions of Company Liquidator:** On receiving an application, the Tribunal shall, by an order, direct the person required to assist or cooperate with the Company Liquidator to comply with the instructions of the Company Liquidator and to cooperate with him in discharging his functions and duties.



17. SETTLEMENT OF LIST OF CONTRIBUTORIES AND APPLICATION OF ASSETS [SECTION 285]

- (1) **Action to be taken by Tribunal after passing of winding up order:** As soon as may be after the passing of a winding up order by the Tribunal, the Tribunal shall -

- settle a **list of contributories**,
- cause **rectification of register of members** in all cases where rectification is required in pursuance of this Act, and
- shall cause the **assets of the company to be applied for the discharge** of its liability.

Provided that where it appears to the Tribunal that it would not be necessary to make calls on or adjust the rights of contributories, the Tribunal may dispense with the settlement of a list of contributories.

- (2) **Identifying contributories on the basis of nature of rights:** In settling the list of contributories, the Tribunal shall distinguish between those who are contributories in their own right and those who are contributories as being representatives of, or liable for the debts of, others.

- (3) **Persons liable to contribute to the assets if certain conditions are fulfilled:** While settling the list of contributories, the Tribunal shall include every person, who is or has been a member, who shall be liable to contribute to the assets of the company an amount sufficient for payment of the debts and liabilities and the costs, charges and expenses of winding up, and for the adjustment of the rights of the contributories among themselves, subject to the following conditions, namely:—

Sl. No.	Liabilities	Conditions for the liabilities to contribute towards the assets
1.	a person who has been a member shall not be liable to contribute	If he has ceased to be a member for the preceding one year or more before the commencement of the winding up
2.	a person who has been a member shall not be liable to contribute in respect of any debt or liability of the company	If such debt or liability contracted after he ceased to be a member
3.	a person who has been a member shall be liable to contribute	When it appears to the Tribunal that the present members are unable to satisfy the contributions required to be made by them in pursuance of this Act
4.	in the case of a company limited by shares	no contribution shall be required from any person, who is or has been a member exceeding the amount, if any, unpaid on

		the shares in respect of which he is liable as such member;
5.	in the case of a company limited by guarantee	if the company has a share capital, such member shall be liable to contribute to the extent of any sum unpaid on any shares held by him as if the company were a company limited by shares.



18. OBLIGATIONS OF DIRECTORS AND MANAGERS [SECTION 286]

Contribution by a Director or Manager whose liability is unlimited: In the case of a limited company, any person who is or has been a director or manager, whose liability is unlimited under the provisions of this Act, shall, in addition to his liability, if any, to contribute as an ordinary member, be liable to make a further contribution as if he were at the commencement of winding up, a member of an unlimited company.

Provided that —

- (a) **A Director or Manager who ceased to hold office for a year or more:** A person who has been a director or manager shall not be liable to make such further contribution, if he has ceased to hold office for a year or upwards before the commencement of the winding up;
- (b) **A Director or Manager not liable to contribute any debt / liability of the company after he ceased to hold office:** A person who has been a director or manager shall not be liable to make such further contribution in respect of any debt or liability of the company contracted after he ceased to hold office;
- (c) **A Director or Manager not liable make further contribution unless Tribunal deems it necessary for satisfying the debts and liabilities:** Subject to the articles of the company, a director or manager shall not be liable to make such further contribution unless the Tribunal deems it necessary to require the contribution in order to satisfy the debts and liabilities of the company, and the costs, charges and expenses of the winding up.



19. ADVISORY COMMITTEE [SECTION 287]

- (1) **Tribunal to direct for appointment of Advisory Committee:** The Tribunal may, while passing an order of winding up of a company, direct that there shall be, **an advisory committee to advise the Company Liquidator and to report to the Tribunal** on such matters as the Tribunal may direct.
- (2) **Composition of Advisory Committee:** The advisory committee appointed by the Tribunal shall consist of **not more than twelve members**, being-

- **creditors and contributories** of the company, or
- such **other persons** in such proportion

as the Tribunal may, keeping in view the circumstances of the company under liquidation, direct.

- (3) **Conducting of meeting for choosing members of Advisory Committee:** The Company Liquidator shall convene a meeting of creditors and contributories, as ascertained from the books and documents, of the company **within thirty days from the date of order of winding up** for enabling the Tribunal to determine the persons who may be members of the advisory committee.
- (4) **Right of Advisory Committee to inspect:** The advisory committee shall have **the right to inspect** the books of account and other documents, assets and properties of the company under liquidation at a reasonable time.
- (5) **Prescribing of Procedure for the conduct of meeting, etc.:** The provisions relating to the convening of the meetings, the procedure to be followed thereat and other matters relating to conduct of business by the advisory committee shall be such as may be prescribed.
- (6) **Company Liquidator to be Chairperson:** The meeting of advisory committee shall be **chaired by the Company Liquidator**.

Example 2: The winding up process is initiated against Premier Merchandise Ltd. An advisory committee is formed by the Tribunal consisting of thirteen members in order to advise the company liquidator and report to the Tribunal on the matters directed by the Tribunal. The composition of Advisory Committee includes seven creditors and six contributories. The said constitution of Advisory Committee is invalid. As per Section 287(2), an Advisory Committee cannot have more than twelve members.



20. SUBMISSION OF PERIODICAL REPORTS TO TRIBUNAL [SECTION 288]

- (1) **Periodical reports for submission to Tribunal:** The Company Liquidator shall make periodical reports to the Tribunal and in any case make a **report at the end of each quarter** with respect to the progress of the winding up of the company in such form and manner as may be prescribed.
- (2) **Review of its orders by Tribunal:** The Tribunal may, on an **application by the Company Liquidator**, review the orders made by it and make such modifications as it thinks fit.



21. POWERS AND DUTIES OF COMPANY LIQUIDATOR [SECTION 290]

- (1) **Powers of Company Liquidator:** Subject to directions by the Tribunal, if any, in this regard, the Company Liquidator, in a winding up of a company by the Tribunal, shall have the power—
- (a) to **carry on the business** of the company so far as may be necessary for the beneficial winding up of the company;
 - (b) to **do all acts and to execute**, in the name and on behalf of the company, all deeds, receipts and other documents, and for that purpose, to use, when necessary, the company's seal;
 - (c) to **sell the immovable and movable property and actionable claims** of the company by public auction or private contract, with power to transfer such property to any person or body corporate, or to sell the same in parcels;
 - (d) to **sell the whole of the undertaking** of the company as a going concern;
 - (e) to **raise any money** required on the security of the assets of the company;
 - (f) to **institute or defend any suit**, prosecution or other legal proceeding, civil or criminal, **in the name and on behalf of the company**;
 - (g) to **invite and settle claim of creditors, employees or any other claimant** and distribute sale proceeds in accordance with priorities established under this Act;
 - (h) to **inspect the records** and returns of the company on the files of the Registrar or any other authority;
 - (i) to **prove rank and claim in the insolvency** of any contributory for any balance against his estate, and to receive dividends in the insolvency, in respect of that balance, as a separate debt due from the insolvent, and rateably with the other separate creditors;
 - (j) to **draw, accept, make and endorse any negotiable instruments** including cheque, bill of exchange, hundi or promissory note in the name and on behalf of the company, with the same effect with respect to the liability of the company as if such instruments had been drawn, accepted, made or endorsed by or on behalf of the company in the course of its business;
 - (k) to **take out, in his official name, letters of administration** to any deceased contributory, and to do in his official name any other act necessary for obtaining payment of any money due from a contributory or his estate which cannot be conveniently done in the name of the company, and in all such cases, the money due shall, for the purpose of enabling the Company Liquidator to take out the letters of

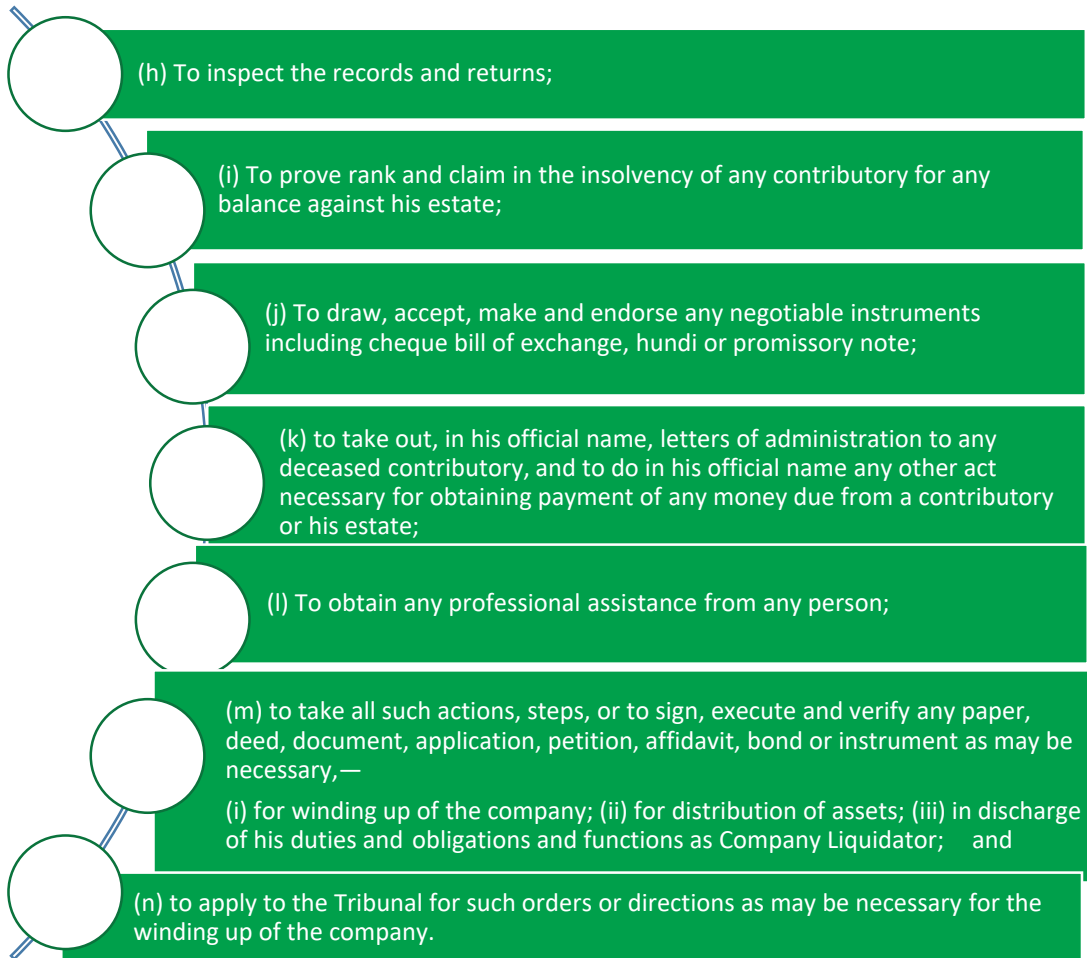
administration or recover the money, be deemed to be due to the Company Liquidator himself;

- (l) **to obtain any professional assistance** from any person or appoint any professional, in discharge of his duties, obligations and responsibilities and for protection of the assets of the company, appoint an agent to do any business which the Company Liquidator is unable to do himself;
- (m) **to take all such actions, steps, or to sign, execute and verify any paper, deed, document**, application, petition, affidavit, bond or instrument as may be necessary,—
 - (i) for winding up of the company;
 - (ii) for distribution of assets;
 - (iii) in discharge of his duties and obligations and functions as Company Liquidator; and
- (n) **to apply to the Tribunal for such orders or directions** as may be necessary for the winding up of the company.

POWERS OF COMPANY LIQUIDATOR

- (a) To carry on the business of the company;
- (b) To do all acts and to execute all deeds, receipts and other documents;
- (c) To sell the immovable and movable property and actionable claims of the company by public auction or private contract;
- (d) To sell the whole of the undertaking of the company as a going concern;
- (e) To raise any money;
- (f) To institute or defend any suit, prosecution or other legal proceeding;
- (g) To invite and settle claim of creditors, employees or any other claimant;

POWERS OF COMPANY LIQUIDATOR.....Contd.



- (2) **Powers of Liquidator under overall control of Tribunal:** The exercise of powers by the Company Liquidator shall be subject to the overall control of the Tribunal.
- (3) **Other duties:** The Company Liquidator shall perform such other duties as the Tribunal may specify in this behalf.

1. The High Court of Gujarat, in *Mukund Chemicals (P.) Ltd. (In Liqu) vs. Darshan Health Care (P.) Ltd.* gave the decision as per Section 290 of the Companies Act, 2013. As per the facts, property of company-in-liquidation were sold to company 'NPL' for Rs. 5.05 crore. Later, 'NPL' nominated company 'D' for said property of Company in Liquidation. Whereby the Directors of 'NPL' also submitted declaration cum-affidavit whereby they declared on oath that they have no objection of

registered assignment and deed of conveyance be executed in favour of 'D'. It was also stated in said affidavit that sale consideration of Rs. 5.05 crore was paid by 'D' to 'NPL'. It was laid in the given case that Official Liquidator of company in liquidation was permitted to execute deed of assignment-cum-conveyance in favour of 'D' subject to payment of stamp duty, registration charges and all other expenses incidental to execution and registration thereof by 'D'.

2. As per the order passed by the High Court of Delhi in *Societe Generale vs. Daewoo Motors India Ltd.*, it was held that any claim with regard to Provident Fund dues can only lie before Commissioner, Provident Fund, under relevant statute and any claims raised directly to Official Liquidator for payment of Provident Fund dues are bound to be rejected as company was never obliged to pay workmen any such amounts in first place. There can be no reason in law to place an additional compulsion on Official Liquidator to either process or pursue claims of workmen with Commissioner, Provident Fund, which even company was not obliged to do the same.



22. PROVISION FOR PROFESSIONAL ASSISTANCE TO COMPANY LIQUIDATOR [SECTION 291]

- (1) **Company liquidator may appoint one/more professionals, if permitted by Tribunal:** The Company Liquidator may, with the sanction of the Tribunal, appoint one or more **chartered accountants or company secretaries or cost accountants or legal practitioners or such other professionals** on such terms and conditions, as may be necessary, to assist him in the performance of his duties and functions under this Act.
- (2) **Disclosure of conflict of interest:** Any person appointed under this section shall disclose forthwith to the Tribunal in the prescribed form **any conflict of interest or lack of independence** in respect of his appointment.

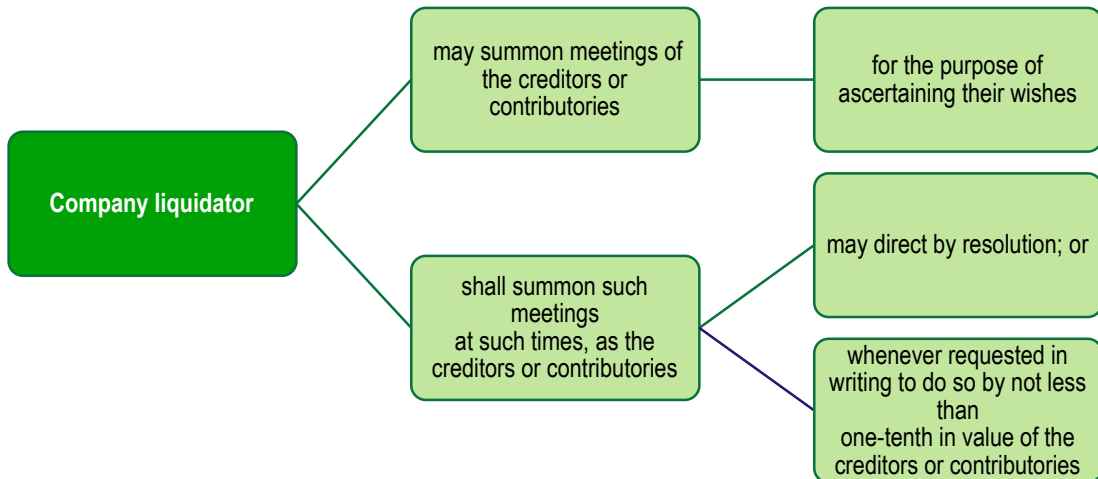


23. EXERCISE AND CONTROL OF COMPANY LIQUIDATOR'S POWERS [SECTION 292]

- (1) **Company Liquidator to follow directions in administration and distribution of assets:** The Company Liquidator shall, in the administration of the assets of the company and the distribution thereof among its creditors, have regard to any directions which may be given by-
 - the resolution of the creditors or contributories at any general meeting, or
 - by the advisory committee.
- (2) **Directions given by creditors or contributories to override directions of Advisory Committee:** Any directions given by the creditors or contributories at any general meeting shall, in case of conflict, be deemed to override any directions given by the advisory committee.

(3) Summons from Company Liquidator: The Company Liquidator—

- (a) may summon meetings of the creditors or contributories, whenever he thinks fit, for the purpose of ascertaining their wishes; and
- (b) shall summon such meetings at such times, as the creditors or contributories, as the case may be, may, by resolution, direct, or whenever requested in writing to do so by not less than one-tenth in value of the creditors or contributories, as the case may be.



- (4) Aggrieved person to apply to Tribunal against the decision of Company Liquidator:** Any person aggrieved by any act or decision of the Company Liquidator may apply to the Tribunal, and the Tribunal may **confirm, reverse or modify the act or decision** complained of and **make such further order** as it thinks just and proper in the circumstances.

24. BOOKS TO BE KEPT BY COMPANY LIQUIDATOR [SECTION 293]

- (1) Company liquidator to maintain proper books for recording entries or minutes:** The Company Liquidator shall keep proper books in such manner, as may be prescribed, in which he shall cause entries or minutes to be made of proceedings at meetings and of such other matters as may be prescribed.
- (2) Inspection of books:** Any creditor or contributory may, subject to the control of the Tribunal, inspect any such books, personally or through his agent.



25. AUDIT OF COMPANY LIQUIDATOR'S ACCOUNTS [SECTION 294]

- (1) **Maintenance of books of accounts:** The Company Liquidator shall **maintain proper and regular books of account** including accounts of receipts and payments made by him in such form and manner as may be prescribed.
- (2) **Presentation of account of receipts and payments to the Tribunal:** The Company Liquidator shall, at such times as may be prescribed but **not less than twice in each year** during his tenure of office, **present to the Tribunal** an account of the receipts and payments as such liquidator in the prescribed form in duplicate, which shall be verified by a declaration in such form and manner as may be prescribed.
- (3) **Audit of accounts:** The Tribunal shall cause the **accounts to be audited** in such manner as it thinks fit, and for the purpose of the audit, the Company Liquidator shall furnish to the Tribunal with such vouchers and information as the Tribunal may require, and the Tribunal may, at any time, require the production of, and inspect, any books of account kept by the Company Liquidator.
- (4) **Filing of copy of audited accounts with Tribunal and Registrar:** When the accounts of the company have been audited, **one copy thereof shall be filed by the Company Liquidator** with the Tribunal, and **the other copy shall be delivered to the Registrar** which shall be **open to inspection** by any creditor, contributory or person interested.
- (5) **Action to be taken when accounts relate to a Government Company:** Where an account referred to in sub-section (4) relates to a Government company, the **Company Liquidator shall forward a copy** thereof—
 - (a) **to the Central Government**, if that Government is a member of the Government company; or
 - (b) **to any State Government**, if that Government is a member of the Government company; or
 - (c) **to the Central Government** and any State Government, if both the Governments are members of the Government company.
- (6) **Summary of accounts to be communicated to every creditor and contributory:** The Company Liquidator shall cause the accounts when audited, or a **summary** thereof, to be **printed**, and shall send a printed copy of the accounts or summary thereof by post to **every creditor and every contributory**.

Note: The Tribunal may dispense with the compliance of the provisions of this sub-section in any case it deems fit.



26. PAYMENT OF DEBTS BY CONTRIBUTORY AND EXTENT OF SET-OFF [SECTION 295]

- (1) **Tribunal to pass an order to pay any money due:** The Tribunal may, at any time after passing of a winding up order, **pass an order** requiring any contributory for the time being on the list of contributories **to pay**, in the manner directed by the order, **any money due to the company**, from him or from the estate of the person whom he represents, exclusive of any money payable by him or the estate by virtue of any call in pursuance of this Act.
- (2) **Order of Tribunal may allow set off:** The Tribunal may while making the above order:—

in the case of an unlimited company	allow to the contributory, by – • way of set-off, any money due to him, or • to the estate which he represents, from the company, on any independent dealing or contract with the company. But not any money due to him as a member of the company in respect of any dividend or profit;
in the case of a limited company	allow to any director or manager whose liability is unlimited, or to his estate, such set-off.

- (3) **Payment of money due against any subsequent call may be allowed to be set off:** In the case of any company (whether limited or unlimited), when all the creditors have been paid in full, any money due on any account, from the company to a contributory, may be allowed to him by way of set-off against any subsequent call.



27. POWER OF TRIBUNAL TO MAKE CALLS [SECTION 296]

The Tribunal may, at any time after the passing of a winding up order, and either before or after it has ascertained the sufficiency of the assets of the company—

- (a) **make calls on all or any of the contributories** for the time being on the list of the contributories, to the extent of their liability, for payment of any money which the Tribunal considers necessary to satisfy the debts and liabilities of the company, and the costs, charges and expenses of winding up, and for the adjustment of the rights of the contributories among themselves; and
- (b) **make an order for payment of any calls**, so made.



28. ADJUSTMENT OF RIGHTS OF CONTRIBUTORIES [SECTION 297]

The Tribunal shall adjust the rights of the contributories among themselves and distribute any surplus among the persons entitled thereto.



29. POWER TO ORDER COSTS [SECTION 298]

Where assets of a company are insufficient to satisfy its liabilities: The Tribunal may, in the event of the assets of a company being insufficient to satisfy its liabilities, **make an order for the payment out of the assets, of the costs, charges and expenses incurred in the winding up**, in such order of priority inter se as the Tribunal thinks just and proper.



30. POWER TO SUMMON PERSONS SUSPECTED OF HAVING PROPERTY OF COMPANY, ETC. [SECTION 299]

(1) **Summon by Tribunal:** The Tribunal may,

- at any time **after the appointment** of a provisional liquidator, or
- the **passing of a winding up order**,

Summon before it –

- any officer of the company or
- person known or
- suspected to have in his possession any property or books or papers, of the company, or
- known or suspected to be indebted to the company, or
- any person whom the Tribunal thinks to be capable of giving information

concerning the promotion, formation, trade, dealings, property, books or papers, or affairs of the company.

(2) **Examination of any person by Tribunal:** The Tribunal may examine any officer or person so summoned on oath concerning the matters aforesaid, either by –

- word of mouth or
- on written interrogatories or
- on affidavit and

may, in the first case, reduce his answers to writing and require him to sign them.

- (3) **Production of books and papers:** The Tribunal may require any officer or person so summoned to produce any books and papers relating to the company in his custody or power, but, where he claims any lien on books or papers produced by him, the production shall be without prejudice to such lien, and the Tribunal shall have power to determine all questions relating to that lien.
- (4) **Liquidator to file a report in respect of debt or property of the company:** The Tribunal may direct the liquidator to file before it a report in respect of debt or property of the company in possession of other persons.
- (5) **Tribunal may order an indebted person to pay money or a person to deliver company's property if he possesses it:** If the Tribunal finds that—
 - (a) a **person is indebted to the company**, the Tribunal may order him to pay to the provisional liquidator or, as the case may be, the liquidator at such time and in such manner as the Tribunal may consider just, the amount in which he is indebted, or any part thereof, either in full discharge of the whole amount or not, as the Tribunal thinks fit, with or without costs of the examination;
 - (b) a **person is in possession of any property belonging to the company**, the Tribunal may order him to deliver to the provisional liquidator or, as the case may be, the liquidator, that property or any part thereof, at such time, in such manner and on such terms as the Tribunal may consider just.
- (6) **Imposition of cost if a summoned person fails to appear:** If any officer or person so summoned fails to appear before the Tribunal at the time appointed without a reasonable cause, the Tribunal may impose an appropriate cost.
- (7) **Execution of order:** Every order made under sub-section (5) shall be executed in the same manner as decrees for the payment of money or for the delivery of property under the Code of Civil Procedure, 1908.
- (8) **Discharge of liability:** Any person making any payment or delivery in pursuance of an order made under sub-section (5) shall by such payment or delivery be, unless otherwise directed by such order, discharged from all liability whatsoever in respect of such debt or property.



31. POWER TO ORDER EXAMINATION OF PROMOTERS, DIRECTORS, ETC. [SECTION 300]

- (1) **Power of Tribunal to order the person to attend and be examined:** Where an order has been made for the winding up of a company by the Tribunal, and the Company Liquidator has made a report to the Tribunal under this Act, stating that in his opinion a fraud has been committed by any person in the promotion, formation, business or conduct of affairs of the company since its formation, the Tribunal may, after considering the report, direct that—

- **such person or officer shall attend** before the Tribunal on a day appointed by it for that purpose, and
 - **be examined** as to the promotion or formation or the conduct of the business of the company or as to his conduct, and
 - **dealings** as an officer thereof.
- (2) **Participation of Company Liquidator in the examination:** The Company Liquidator shall take part in the examination, and for that purpose he or it may, if specially authorised by the Tribunal in that behalf, employ such legal assistance as may be sanctioned by the Tribunal.
- (3) **Examination on oath:** The person shall be examined on oath and shall answer all such questions as the Tribunal may put, or allow to be put, to him.
- (4) **Rights available to the person who is to be examined:** A person ordered to be examined under this section—
- (a) shall, before his examination, **be furnished at his own cost with a copy of the report** of the Company Liquidator; and
 - (b) **may at his own cost employ chartered accountants or company secretaries or cost accountants or legal practitioners** entitled to appear before the Tribunal under section 432, who shall be at liberty to put to him such questions as the Tribunal may consider just for the purpose of enabling him to explain or qualify any answers given by him.
- (5) **Appearance of Company Liquidator on hearing of an application made by person to be exculpated from any charges:** If any such person applies to the Tribunal to be exculpated from any charges made or suggested against him, it shall be the duty of the Company Liquidator to appear on the hearing of such application and call the attention of the Tribunal to any matters which appear to the Company Liquidator to be relevant.
- (6) **Order for payment of costs:** If the Tribunal, after considering any evidence given or hearing witnesses called by the Company Liquidator, allows the application made under sub-section (5), the Tribunal may order payment to the applicant of such costs as it may think fit.
- (7) **Records of examination in writing:** Notes of the examination shall be taken down in writing, and shall be read over to or by, and signed by, the person examined, a copy be supplied to him and may thereafter be used in evidence against him, and shall be open to inspection by any creditor or contributory at all reasonable times.
- (8) **Adjournment:** The Tribunal may, if it thinks fit, adjourn the examination from time to time.
- (9) **Examination can be before any person / authority if the Tribunal so directs:** An examination under this section may, if the Tribunal so directs, be held before any person or authority authorised by the Tribunal.

- (10) **Exercise of powers of Tribunal by the concerned person / authority:** The powers of the Tribunal under this section as to the conduct of the examination, but not as to costs, may be exercised by the person or authority before whom the examination is held in pursuance of sub-section (9).



32. ARREST OF PERSON TRYING TO LEAVE INDIA OR ABSCOND [SECTION 301]

At any time either before or after passing a winding up order, if the Tribunal is satisfied that a contributory or a person having property, accounts or papers of the company in his possession is about to leave India or otherwise to abscond, or is about to remove or conceal any of his property, for the purpose of evading payment of calls or of avoiding examination respecting the affairs of the company, the Tribunal may cause—

- (a) the contributory to be detained until such time as the Tribunal may order; and
- (b) his books and papers and movable property to be seized and safely kept until such time as the Tribunal may order.

Any time either before or after passing a winding up order, if the Tribunal is satisfied that -

- a contributory, or
- a person having property, accounts or papers of the company in his possession

is about-

- to leave India or
- otherwise to abscond, or
- is about to remove or conceal any of his property, for evading payment of calls, or
- of avoiding examination respecting the affairs of the company,

the Tribunal may cause—

- the contributory to be detained until such time as the Tribunal may order; and
- his books and papers and movable property to be seized and safely kept until such time as the Tribunal may order.



33. DISSOLUTION OF COMPANY BY TRIBUNAL [SECTION 302]

S. No.	Conditions	Rights consequent to prevailing conditions
1.	When the affairs of a company have been completely wound up	the Company Liquidator shall make an application to the Tribunal for dissolution of such company.
2.	The Tribunal shall on an application filed by the Company Liquidator, or when the Tribunal is of the opinion that it is just and reasonable in the circumstances that an order for the dissolution of the company should be made	The Tribunal shall make an order that the company be dissolved from the date of the order, and the company shall be dissolved accordingly.
3.	Tribunal shall, within thirty days from the date of order forward the copy of order to Registrar.	Registrar shall record in the register relating to the company a minute of the dissolution of the company, and direct the Company Liquidator to forward a copy of the order to the Registrar who shall record in the register relating to the company a minute of the dissolution of the company.

The High Court of Madhya Pradesh in *Alpine Biotech Ltd., In Re*, in the light of Section 302 of the Companies Act, 2013 gave the decision on the Dissolution of company. As per the fact, on the basis of reference received from BIFR, winding up order of applicant company was passed. Official Liquidator (OL) was appointed. In pursuance to order of court, assets of company in liquidation were sold by secured creditor under provisions of the SARFAESI Act, 2002 in association with OL in auction and possession of assets was handed over to successful auction purchaser. Since all assets of company in liquidation were sold, OL called meetings of secured creditors to ascertain assets/properties of company in liquidation if any left. However, no secured creditor attended said meeting. In such circumstances, Official Liquidator filed instant application for purpose of passing of final order in respect of dissolution of company in liquidation. Court laid down that since all assets of company in liquidation had already been sold and no assets were left, it was just and appropriate to dissolve company.



34. APPEALS FROM ORDERS MADE BEFORE COMMENCEMENT OF ACT [SECTION 303]

Retrospective effect: Nothing in this Chapter shall affect the operation or enforcement of any order made by any Court in any proceedings for the winding up of a company immediately before the commencement of this Act and an appeal against such order shall be filed before such authority competent to hear such appeals before such commencement.

The High Court of Delhi in *R.K. Aggarwal V. Official Liquidator* came out with a decision on appeals from orders made before commencement of Act. It held that though an erstwhile shareholder of a company in liquidation is entitled to appeal but not ex-director. Even where appellant in affidavit had described himself as ex-director, even though appeal contained an averment that he held 75 % of shares of company in liquidation, appeal would not be maintainable.

(PART II- VOLUNTARY WINDING UP) SECTIONS 304- 323 (OMITTED)

Provisions dealing with voluntary winding up under the Companies Act, 2013 stand omitted due to Section 255 of Insolvency and Bankruptcy Code, 2016 and section 59 which deals with voluntary winding up covered under Chapter V of Insolvency & Bankruptcy Code, 2016 has been notified on 01.04.2017.

PART III—PROVISIONS APPLICABLE TO EVERY MODE OF WINDING UP



35. DEBTS OF ALL DESCRIPTIONS TO BE ADMITTED TO PROOF [SECTION 324]

In every winding up (subject, in the case of insolvent companies, to the application in accordance with the provisions of this Act or of the law of insolvency), -

- **all debts** payable on a contingency, and
- **all claims** against the company, present or future, certain or contingent, ascertained or sounding only in damages,

shall be admissible to proof against the company, a just estimate being made, so far as possible, of the value of such debts or claims as may be subject to any contingency, or may sound only in damages, or for some other reason may not bear a certain value.



36. OVERRIDING PREFERENTIAL PAYMENTS [SECTION 326]

(1) **Debts to be paid in priority:** In the winding up of a company under this Act, the following debts shall be paid in priority to all other debts:—

- (a) **workmen's dues;** and
- (b) where a **secured creditor** has realised a secured asset, so much of the debts due to such secured creditor as could not be realised by him or the amount of the workmen's portion in his security (if payable under the law), **whichever is less**, *pari passu* with the workmen's dues.

Provided that in case of the winding up of a company, the sums referred to in sub-clauses (i) and (ii) of clause (b) of the *Explanation* (given below), which are payable for a period of 2 years preceding the winding up order or such other period as may be prescribed, shall be paid in priority to all other debts (including debts due to secured creditors), within a period of 30 days of sale of assets and shall be subject to such charge over the security of secured creditors as may be prescribed.

(2) **Debts mentioned in Proviso to be paid in full:** The debts payable under the proviso to subsection (1) shall be paid in full before any payment is made to secured creditors and thereafter debts payable under that subsection shall be paid in full, unless the assets are insufficient to meet them, in which case they shall abate in equal proportions.

Example 3: The value of the security of a secured creditor of a company is ₹ 1,00,000. The total amount of the workmen's dues is ₹ 1,00,000. The amount of the debts due from the company to its secured creditors is ₹ 3,00,000. The aggregate of the amount of workmen's dues and the amount of debts due to secured creditors is ₹ 4,00,000. The workmen's portion of the security is, therefore, one-fourth of the value of the security, that is ₹ 25,000.

Explanation—For the purposes of this section, and section 327—

- (a) **"workmen"**, in relation to a company, means the employees of the company, being workmen within the meaning of clause (s) of section 2 of the Industrial Disputes Act, 1947;
- (b) **"workmen's dues"**, in relation to a company, means the aggregate of the following sums due from the company to its workmen, namely:—
 - (i) all **wages or salary** including wages payable for time or piece work and salary earned wholly or in part by way of commission of any workman in respect of services rendered to the company and any compensation payable to any workman under any of the provisions of the Industrial Disputes Act, 1947.
 - (ii) all accrued **holiday remuneration** becoming payable to any workman or, in the case of his death, to any other person in his right on the termination of his employment before or by the effect of the winding up order or resolution;

- (iii) unless the **company is being wound up voluntarily merely for the purposes of reconstruction or amalgamation with another company** or unless the company has, at the commencement of the winding up, under such a contract with insurers as is mentioned in section 14 of the Workmen's Compensation Act, 1923 (19 of 1923), rights capable of being transferred to and vested in the workmen, all amount due in respect of any compensation or liability for compensation under the said Act in respect of the death or disablement of any workman of the company;
- (iv) all **sums due to any workman** from the provident fund, the pension fund, the gratuity fund or any other fund for the welfare of the workmen, maintained by the company;
- (c) **"workmen's portion"**, in relation to the security of any secured creditor of a company, means the amount which bears to the value of the security the same proportion as the amount of the workmen's dues bears to the aggregate of the amount of workmen's dues and the amount of the debts due to the secured creditors.

The High Court of Bombay, *Kamani Employee's Union V. Official Liquidator and Liquidator of Kma Ltd. (In Liquidation)* gave a decision in the light of the sections Section 326 of the Companies Act, 2013.

In the given case, Kamani Employees Union(Appellant) was a registered trade union of the employees of the company-in-liquidation. KMA Workers and Staff Union (respondent No.2) was a rival trade union.

As the business of the company became unviable, the company was referred to the Board for Industrial and Financial Reconstruction (BIFR) in a *suo motu* reference. By an order dated 6-9-2000, BIFR recommended winding up of the company.

Later, a consent order was passed for sale of assets of company and sale proceeds were deposited in no lien account. Industrial Court and DRT adjudicated claims of workmen, banks and financial institutions. Appellant-employees union challenged order passed by Industrial Court and DRT.

Pursuant to negotiations, consent terms were executed between Union and banks some workmen did not join in consent terms. Company Court ordered winding up of company on 24-10-2008. By a further order dated 13-3-2019, Company Court accepted consent terms and authorized payments to be made in accordance with consent terms. Appellant filed application seeking a direction against Official Liquidator for adjudication of claims of workmen and secured creditors of company in accordance with sections 326. Company Judge by impugned order held that dissenting workmen were not bound by consent terms dated 8-7-2008 and that dissenting workmen were entitled to wages up to date of winding up order, i.e., 24-10-2008. It was held that dissenting workmen could not be deprived of their statutory and legitimate right to participate in product of their labour and effort, which became disbursable, in wake of winding up, on basis of such submissions of tacit consent or waiver and, therefore, finding recorded by Company Judge that consent terms did not bind dissenting workmen.

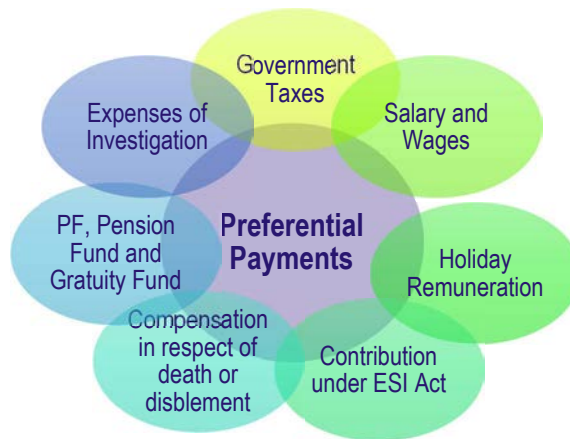


37. PREFERENTIAL PAYMENTS [SECTION 327]

(1) In a winding up, subject to the provisions of section 326, there shall be paid in priority to all other debts,—

- (a) all **revenues, taxes, cesses and rates** due from the company to the Central Government or a State Government or to a local authority at the relevant date, and having become due and payable within the 12 months immediately before that date;
- (b) all **wages or salary** including wages payable for time or piece work and salary earned wholly or in part by way of commission of any employee in respect of services rendered to the company and due for a period not exceeding 4 months within the 12 months immediately before the relevant date, subject to the condition that the amount payable under this clause to any workman shall not exceed such amount as may be notified;
- (c) all **accrued holiday remuneration** becoming payable to any employee, or in the case of his death, to any other person claiming under him, on the termination of his employment before, or by the winding up order, or, as the case may be, the dissolution of the company;
- (d) unless the company is being wound up voluntarily merely for the purposes of reconstruction or amalgamation with another company, **all amount due in respect of contributions** payable during the period of 12 months immediately before the relevant date by the company as the employer of persons under the Employees' State Insurance Act, 1948 or any other law for the time being in force;
- (e) unless the company has, at the commencement of winding up, under such a contract with any insurer as is mentioned in section 14 of the Workmen's Compensation Act, 1923, rights capable of being transferred to and vested in the workmen, **all amount due in respect of any compensation or liability for compensation** under the said Act in respect of the death or disablement of any employee of the company;

Provided that where any compensation under the said Act is a weekly payment, the amount payable under this clause shall be taken to be the amount of the lump sum for which such weekly payment could, if redeemable, be redeemed, if the employer has made an application under that Act;
- (f) **all sums due to any employee from the provident fund, the pension fund, the gratuity fund or any other fund** for the welfare of the employees, maintained by the company; and
- (g) the **expenses of any investigation** held in pursuance of sections 213 and 216, in so far as they are payable by the company.



(2) **Right of person advancing money for making certain payments:** Where any payment has been made to any employee of a company on account of -

- **wages or salary**, or
- **accrued holiday remuneration**, himself or,
- in the case of his **death**, to **any other person claiming** through him,

out of **money advanced** by some person for that purpose, the person by whom the money was advanced shall, in a winding up, have a right of priority in respect of the money so advanced and paid-up to the amount by which the sum in respect of which the employee or other person in his right would have been entitled to priority in the winding up has been reduced by reason of the payment having been made.

(3) **Debts to rank equally among themselves keeping in view the available assets:** The debts enumerated in this section shall—

- (a) **rank equally among themselves and be paid in full**, unless the assets are insufficient to meet them, in which case they shall abate in equal proportions; and
- (b) so far as the assets of the company available for payment to general creditors are insufficient to meet them, have **priority over the claims of holders of debentures** under any floating charge created by the company, and be paid accordingly out of any property comprised in or subject to that charge.

(4) **Debts to be discharged forthwith if assets are sufficient to meet them:** Subject to the retention of such sums as may be necessary for the costs and expenses of the winding up, the debts under this section shall be discharged forthwith so far as the assets are sufficient to meet them, and in the case of the debts to which priority is given under clause (d) of sub-

section (1), formal proof thereof shall not be required except in so far as may be otherwise prescribed.

- (5) **Debts to which priority is given shall be a first charge on the goods or effects distrained on:** In the event of a landlord or other person distraining or having distrained on any goods or effects of the company **within three months** immediately before the date of a winding up order, the debts to which priority is given under this section **shall be a first charge on the goods or effects** so distrained on or the proceeds of the sale thereof:

Provided that, in respect of any money paid under any such charge, the landlord or other person shall have the same rights of priority as the person to whom the payment is made.

- (6) **Remuneration for holiday / absence from work to be deemed to be wages:** Any remuneration in respect of a period of holiday or of absence from work on medical grounds through sickness or other good cause shall be deemed to be wages in respect of services rendered to the company during that period.
- (7) **Non-applicability of sections 326 & 327:** Sections 326 and 327 shall not be applicable in the event of liquidation under the Insolvency and Bankruptcy Code, 2016.

Explanation—For the purposes of this section,—

- (a) the expression **“accrued holiday remuneration”** includes, in relation to any person,
- all sums which, by virtue either of his contract of employment or of any enactment including any order made or direction given thereunder,
 - are payable on account of the remuneration which would, in the ordinary course, have become payable to him in respect of a period of holiday, had his employment with the company continued until he became entitled to be allowed the holiday;
- (b) the expression **“employee”** does not include a workman; and
- (c) the expression **“relevant date”** means in the case of a company being wound up by the Tribunal-
- the date of appointment or first appointment of a provisional liquidator, or
 - if no such appointment was made, the date of the winding up order,
- unless, in either case, the company had commenced to be wound up voluntarily before that date under the Insolvency and Bankruptcy Code, 2016;



38. FRAUDULENT PREFERENCE [SECTION 328]

- (1) **When any transaction may be treated as fraudulent preference:** Where a company has given preference to a person who is-

- **one of the creditors** of the company, or
- **a surety or guarantor** for any of the debts or other liabilities of the company,

and the company does anything or suffers anything done which has the effect of putting that person into a position which, in the event of the company going into liquidation, will be better than the position he would have been in if that thing had not been done prior to 6 months of making winding up application, the Tribunal, if satisfied that, such transaction is a fraudulent preference may order as it may think fit for restoring the position to what it would have been if the company had not given that preference.

(2) Order of Tribunal may declare a transaction as invalid in case of fraudulent preference:

If the Tribunal is satisfied that there is a-

- preference transfer of property, movable or immovable, or
- any delivery of goods,
- payment,
- execution made, taken or done by or against a company within 6 months before making winding up application,

the Tribunal may order as it may think fit and may declare such transaction invalid and restore the position.

The Supreme Court of India in *IDBI Bank Ltd. v. Official Liquidator*, held that a transfer or any other act done in relation to property of a company within a period of six months before commencement of its winding up, shall be deemed to be a fraudulent preference of its creditors and accordingly be held invalid,



39. TRANSFERS NOT IN GOOD FAITH TO BE VOID [SECTION 329]

Any **transfer of property**, movable or immovable, or **any delivery of goods**, made by a company, not being –

- a transfer or delivery made **in the ordinary course of its business**, or
- in **favour of a purchaser or encumbrancer in good faith** and for **valuable consideration**,

if made within a period of **one year before the presentation** of a petition for winding up by the Tribunal, shall be **void against the Company Liquidator**.

The High Court of Delhi in *Reserve Bank of India v. JVG Finance Ltd.* passed an order under section 329 of the Companies Act, 2013. In the given case, applicant purchased certain lands from five companies of JVG Group through a authorised signatory and ex-director of JVG Group of companies during period from May 2002 to July 2002.

Entire consideration had been paid in cash allegedly to 'authorized signatory' and agreement to sell was duly registered with appropriate authorities during that period. Thereafter seller companies had gone into liquidation and on 3-9-2002, court directed that prior to affecting any sale, alienation, transfer or creation of any third party interest in any assets of said companies, permission of court should be obtained.

Hence, applicant filed application for grant of permission to complete process of registration/execution of sale deeds.

Court appointed a one man committee (Thareja Committee) for verifying claim of applicant. Thareja committee report concluded that relevant documents, namely, cash book, ledger, etc., had not been placed on record and transaction lacked *bona-fidely*. Further, SFIO also investigated into matter and found that 'authorised signatory' was never authorised to effect said transaction on behalf of five companies and secondly, he had acted in a fraudulent manner and had sought to siphon off funds of said companies by indulging in those transactions. It was held by the court that said transaction was carried out only to whisk away valuable assets of JVG Group of companies which at that time were likely to go under winding up proceedings, hence application filed by applicant was liable to be dismissed and could not be granted permission to complete process of registration/execution of sale deeds of land.



40. CERTAIN TRANSFERS TO BE VOID [SECTION 330]

Any **transfer or assignment** by a company of all its **properties or assets** to **trustees** for the benefit of all its creditors shall **be void**.



41. LIABILITIES AND RIGHTS OF CERTAIN PERSONS FRAUDULENTLY PREFERRED [SECTION 331]

- (1) **Determination of rights and liabilities of fraudulently preferred persons:** Where a company is being wound up and anything made, taken or done after the commencement of this Act is invalid under section 328 as a fraudulent preference of a person interested in property mortgaged or charged to secure the company's debt, then, without prejudice to any rights or liabilities arising, apart from this provision, the person preferred shall be subject to the same liabilities, and shall have the same rights, as if he had undertaken to be personally liable as a surety for the debt,-

- to the extent of the mortgage or charge on the property,
- or
- the value of his interest,

Whichever is less

- (2) **Value of interest shall be determined as at the date of the transaction constituting the fraudulent preference:** The value of the interest of the person preferred under sub-section (1) shall be determined as at the date of the transaction constituting the fraudulent preference, as if the interest were free of all encumbrances other than those to which the mortgage or charge for the debt of the company was then subject.
- (3) **Application to Tribunal:** On an application made to the Tribunal with respect to any payment on the ground that the payment was a fraudulent preference of a surety or guarantor, the Tribunal shall have jurisdiction to determine any questions with respect to the payment arising between the person to whom the payment was made and the surety or guarantor and to grant relief in respect thereof, notwithstanding that it is not necessary so to do for the purposes of the winding up, and for that purpose, may give leave to bring in the surety or guarantor as a third party as in the case of a suit for the recovery of the sum paid.
- (4) The provisions of sub-section (3) shall apply *mutatis mutandis* in relation to transactions other than payment of money.



42. EFFECT OF FLOATING CHARGE [SECTION 332]

The provisions of section 332 of the Companies Act, 2013 stop an **insolvent company** from creating floating charge on its assets. Accordingly:

Where a company is being wound up,

- a **floating charge** on the undertaking or property of the company created within the 12 months immediately preceding the commencement of the winding up,

shall, unless it is proved that the company immediately after the creation of the charge was solvent, **be invalid**, except for the amount of any cash paid to the company at the time of, or subsequent to the creation of, and in consideration for, the charge, together with interest on that amount at the rate of 5% per annum or such other rate as may be notified by the Central Government in this behalf.



43. DISCLAIMER OF ONEROUS PROPERTY [SECTION 333]

- (1) **Disclaiming of certain property by Company Liquidator:** Where any part of the property of a company which is being wound up consists of—

(a) land of any tenure, burdened with onerous covenants;

(b) shares or stocks in companies;

(c) any other property which is not saleable or is not readily saleable by reason of the possessor thereof being bound either to the performance of any onerous act or to the payment of any sum of money; or

(d) unprofitable contracts,

the Company Liquidator may, notwithstanding that he has endeavoured to sell or has taken possession of the property or exercised any act of ownership in relation thereto or done anything in pursuance of the contract, with the leave of the Tribunal and subject to the provisions of this section, -

- by writing signed by him, at any time within 12 months after the commencement of the winding up or such extended period as may be allowed by the Tribunal, disclaim the property.

Where the Company Liquidator had not become aware of the existence of any such property within 1 month from the commencement of the winding up, the power of disclaiming the property may be exercised at any time within twelve months after he has become aware thereof or such extended period as may be allowed by the Tribunal.

(2) Determination of rights, interest and liabilities in respect of the property disclaimed:

The disclaimer shall operate to determine, as from the date of disclaimer, the rights, interest and liabilities of the company in or in respect of the property disclaimed, but shall not, except so far as is necessary for the purpose of releasing the company and the property of the company from liability, affect the rights, interest or liabilities of any other person.

(3) Notices to be given to the interested persons: The Tribunal, before or on granting leave to disclaim, may require such notices to be given to persons interested, and impose such terms as a condition of granting leave, and make such other order in the matter as the Tribunal considers just and proper.

(4) Circumstances in which Company Liquidator is not entitled to disclaim any property:

The Company Liquidator shall not be entitled to disclaim any property in any case where an application in writing has been made to him by any person interested in the property requiring him to decide whether he will or will not disclaim and the Company Liquidator has not, within

a period of 28 days after the receipt of the application or such extended period as may be allowed by the Tribunal, give notice to the applicant that he intends to apply to the Tribunal for leave to disclaim, and in case the property is under a contract, if the Company Liquidator after such an application as aforesaid does not within the said period or extended period disclaim the contract, he shall be deemed to have adopted it.

(5) **Power of Tribunal to make order on an application of person who is entitled to benefit of a contract made with company:** The Tribunal may, on the application of any person who is, as against the Company Liquidator, entitled to the benefit or subject to the burden of a contract made with the company, make an order-

- rescinding the contract on such terms as to payment by or to either party of damages for the non-performance of the contract, or
- otherwise as the Tribunal considers just and proper, and
- any damages payable under the order to any such person may be proved by him as a debt in the winding up.

(6) **Power of Tribunal to make order on an application made by any person in certain circumstances:** The Tribunal may, on an application by any person who either claims any interest in any disclaimed property or is under any liability not discharged under this Act in respect of any disclaimed property, and after hearing any such persons as it thinks fit, make an order for the –

- vesting of the property in, or
- the delivery of the property to,
- any person entitled thereto or to whom it may seem just that the property should be delivered by way of compensation for such liability as aforesaid,
- or a trustee for him, and

on such terms as the Tribunal considers just and proper, and on any such vesting order being made, the property comprised therein shall vest accordingly in the person named therein in that behalf without any conveyance or assignment for the purpose:

Where the property disclaimed is of a **leasehold nature**-

the Tribunal shall not make a vesting order in favour of any person claiming under the company, whether as under-lessee or as mortgagee or holder of a charge by way of demise, except upon the terms of making that person—

- (a) subject to the same liabilities and obligations as those to which the company was subject under the lease in respect of the property at the commencement of the winding up; or
- (b) if the Tribunal thinks fit, subject only to the same liabilities and obligations as if the lease had been assigned to that person at that date,

and in either event as if the lease had comprised only the property comprised in the vesting order, and any mortgagee or under-lessee declining to accept a vesting order upon such terms shall be excluded from all interest in, and security upon the property, and,

If there is no person claiming under the company who is willing to accept an order upon such terms, the Tribunal shall have power to vest the estate and interest of the company in the property in any person liable, either personally or in a representative character, and either alone or jointly with the company, to perform the covenants of the lessee in the lease, free and discharged from all estates, encumbrances and interests created therein by the company.

- (7) **Affected person shall be deemed creditor of company:** Any person affected by the operation of a disclaimer under this section shall be deemed to be a creditor of the company to the amount of the compensation or damages payable in respect of such effect, and may accordingly prove the amount as a debt in the winding up.



44. TRANSFERS, ETC., AFTER COMMENCEMENT OF WINDING UP TO BE VOID [SECTION 334]

In the case of a winding up by the Tribunal, any disposition of the property including actionable claims, of the company and any transfer of shares in the company or alteration in the status of its members, made after the commencement of the winding up shall, unless the Tribunal otherwise orders, be void.



45. CERTAIN ATTACHMENTS, EXECUTIONS, ETC., IN WINDING UP BY TRIBUNAL TO BE VOID [SECTION 335]

- (1) **Certain attachments, distress, executions or sale put in force to be void:** Where any company is being wound up by the Tribunal,—
- (a) **any attachment, distress or execution** put in force, without leave of the Tribunal **against the estate or effects of the company**, after the commencement of the winding up; or
 - (b) **any sale held**, without leave of the Tribunal of **any of the properties or effects of the company**, after such commencement of the winding up, shall be void.
- (2) **Section not applicable to proceedings for the recovery of any tax/dues:** Nothing in this section shall apply to any proceedings for the **recovery of any tax or impost or any dues** payable to the Government.

The High Court of Madras in *Zylog Systems Ltd. v. Brainhunter Systems Ltd.* passed an order with respect to section 335 of the Companies Act, 2013. Facts states that applicant company 'Zylog' had

several subsidiaries. A Canadian company 'B' was a wholly owned subsidiary of applicant. Applicant was stated to have invested about Canadian Dollars (CDN) 35 million by way of equity and loan in 'B'.

Some time in the year 2010, 'B' approached ICICI Bank, Canada for a term loan and working capital loan. Based on the request by 'B', loans were sanctioned by ICICI Bank, Canada. In relation thereto, ICICI Bank Canada required standby letters of credit (SBLCs) from ICICI Bank India. For purposes of providing such SBLCs, ICICI Bank India required that applicant be involved in the transaction. Therefore, applicant applied for credit facilities and such facilities were sanctioned by ICICI Bank India on the security of a pledge of its 100 per cent shareholding in 'B'.



46. OFFENCES BY OFFICERS OF COMPANIES IN LIQUIDATION [SECTION 336]

Said offences
committed by
Officers of
Companies

- Non disclosure of assets
- Non delivery of property
- Non delivery of books and papers
- Non delivery of information
- Material omissions
- Prevents the production of any book or paper
- Displays fictitious losses or expenses
- False representation

- (1) **If any person, who is or has been an officer of a company which, at the time of the commission of the alleged offence, is being wound up**, by the Tribunal under this Act or which is subsequently **ordered to be wound up** by the Tribunal under this Act—
- (a) does not, to the best of his knowledge and belief, fully and truly **disclose to the Company Liquidator all the property**, movable and immovable, of the company, and how and to whom and for what consideration and when the company disposed of any part thereof, except such part as has been disposed of in the ordinary course of the business of the company;
 - (b) does not **deliver up to the Company Liquidator**, or as he directs, all such part of the **movable and immovable property** of the company as is in his custody or under his control and which he is required by law to deliver up;
 - (c) does not **deliver up to the Company Liquidator**, or as he directs, all such **books and papers** of the company as are in his custody or under his control and which he is required by law to deliver up;
 - (d) within the 12 months immediately before the commencement of the winding up or at any time thereafter,—

- (i) **conceals any part of the property** of the company to the value of 1,000 rupees or more, or conceals any debt due to or from the company;
- (ii) **fraudulently removes any part of the property** of the company to the value of 1,000 rupees or more;
- (iii) **conceals, destroys, mutilates or falsifies**, or is privy to the concealment, destruction, mutilation or falsification of, **any book or paper** affecting or relating to, the property or affairs of the company;
- (iv) **makes, or is privy to the making of, any false entry** in any book or paper affecting or relating to, the property or affairs of the company;
- (v) **fraudulently parts with, alters or makes any omission in**, or is privy to the fraudulent parting with, altering or making of any omission in, **any book or paper** affecting or relating to the property or affairs of the company;
- (vi) by any **false representation or other fraud, obtains on credit**, for or on behalf of the company, any property which the company does not subsequently pay for;
- (vii) under the **false pretence that the company is carrying on its business, obtains on credit**, for or on behalf of the company, any property which the company does not subsequently pay for; or
- (viii) **pawns, pledges or disposes of any property of the company which has been obtained on credit and has not been paid** for, unless such pawning, pledging or disposing of the property is in the ordinary course of business of the company;
- (e) makes any **material omission in any statement** relating to the affairs of the company;
- (f) knowing or believing that a **false debt** has been proved by any person under the winding up, fails for a period of one month **to inform** the Company Liquidator thereof;
- (g) after the **commencement of the winding up, prevents the production of any book or paper** affecting or relating to the property or affairs of the company;
- (h) after the commencement of the winding up or at any meeting of the creditors of the company within the twelve months next before the commencement of the winding up, **attempts to account for any part of the property of the company by fictitious losses** or expenses; or
- (i) is **guilty of any false representation or fraud** for the purpose of obtaining the consent of the creditors of the company or any of them, to an agreement with reference to the affairs of the company or to the winding up,

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

It shall be a good defence if the accused proves that he had no intent to defraud or to conceal the true state of affairs of the company or to defeat the law.

- (2) **Person who takes in pawn or pledge or otherwise receives the property, knowing it to be pawned, pledged, or disposed of in circumstances under sub-clause (viii) of clause (d) of sub-section (1) shall be punishable:** Where any person pawns, pledges or disposes of any property in circumstances which amount to an offence under sub-clause (viii) of clause (d) of sub-section (1), every person who takes in pawn or pledge or otherwise receives the property, knowing it to be pawned, pledged, or disposed of in such circumstances as aforesaid, shall be punishable with imprisonment for a term which shall not be less than 3 years but which may extend to 5 years and with fine which shall not be less than 3 lakh rupees but which may extend to 5 lakh rupees.

Explanation-For the purposes of this section, the expression “**officer**” includes any person in accordance with whose directions or instructions the directors of the company have been accustomed to act.



47. STATEMENT THAT COMPANY IS IN LIQUIDATION [SECTION 344]

- (1) **Statement that company is being of wound up to be disclosed:** Where a company is being wound up, whether by
- the Tribunal or
 - voluntarily,
- every invoice, order for goods or business letter issued-
- by or on behalf of the company or
 - a Company Liquidator of the company, or
 - a receiver or
 - manager of the property of the company,
- being a document on or in which the name of the company appears, shall contain a statement that the company is being wound up.
- (2) **If a company contravenes the above provisions,** the company, and every officer of the company, the Company Liquidator and any receiver or manager, who willfully authorises or permits the non-compliance, shall be punishable with fine which shall **not be less than fifty thousand rupees** but which may **extend to three lakh rupees**.

Example 4: The Tribunal has initiated the process of winding up against RSJ Ltd. The goods in stock of RSJ Ltd are sold in the normal course of business to PQT Ltd. The liquidator appointed for carrying out the process of winding up compels the management of RSJ Ltd to write ‘The company is being wound up’ on the sales invoice issued by RSJ Ltd. The management opposes the same as

the transaction is in normal course of business. As per the terms of the Section 344 of the Companies Act, 2013, the statement suggested by liquidator is mandatory and must be given due effect otherwise it shall be considered as violation.



48. BOOKS AND PAPERS OF COMPANY TO BE EVIDENCE [SECTION 345]

Books and Papers to be *prima facie* evidence of truth of all matters: Where a company is being wound up, all books and papers of the company and of the Company Liquidator shall, as between the contributories of the company, be prima facie evidence of the truth of all matters purporting to be recorded therein.



49. INSPECTION OF BOOKS AND PAPERS BY CREDITORS AND CONTRIBUTORIES [SECTION 346]

- (1) **Inspection of Books and Papers:** At any time after the making of an order for the winding up of a company by the Tribunal, any creditor or contributory of the company may inspect the books and papers of the company only in accordance with, and subject to such rules as may be prescribed.
- (2) **No restrictions on the rights of certain persons:** Nothing contained in sub-section (1) shall exclude or restrict any rights conferred by any law for the time being in force—
 - (a) on the Central Government or a State Government;
 - (b) on any authority or officer thereof; or
 - (c) on any person acting under the authority of any such Government or of any such authority or officer.



50. DISPOSAL OF BOOKS AND PAPERS OF COMPANY [SECTION 347]

- (1) **Disposal of books and papers as per the directions of Tribunal:** When the affairs of a company have been completely wound up and it is about to be dissolved, the books and papers of such company and those of the Company Liquidator may be disposed of in such manner as the Tribunal directs.
- (2) **No responsibility to devolve after expiry of five years:** After the expiry of five years from the dissolution of the company, no responsibility shall devolve-
 - on the company,
 - the Company Liquidator, or
 - any person

to whom the custody of the books and papers has been entrusted, by reason of any book or paper not being forthcoming to any person claiming to be interested therein.

- (3) The Central Government may, by rules,—
- prevent for such period** as it thinks proper **the destruction of the books and papers** of a company which has been wound up and of its Company Liquidator; and
 - enable any creditor or contributory of the company to make representations** to the Central Government in respect of the matters specified in clause (a) and **to appeal to the Tribunal** from any order which may be made by the Central Government in the matter.
- (4) **Punishment for contravention:** If any person acts in contravention of any rule framed or an order made under sub-section (3), he shall be punishable with fine which may extend to 50,000 rupees.



51. COMPANY LIQUIDATION DIVIDEND AND UNDISTRIBUTED ASSETS ACCOUNT [SECTION 352]

- (1) **Unpaid money in the hands of liquidator to be deposited forthwith into a separate special account:** Where any company is being wound up and the liquidator has in his hands or under his control any money representing—
- dividends payable to any creditor** but which had remained unpaid for 6 months after the date on which they were declared; or
 - assets refundable to any contributory** which have remained undistributed for 6 months after the date on which they become refundable,
- the liquidator shall forthwith deposit the said money into a separate special account to be known as the Company Liquidation Dividend and Undistributed Assets Account maintained in a scheduled bank.
- (2) **Transfer of money into the Company Liquidation Dividend and Undistributed Assets Account:** The liquidator shall, on the dissolution of the company, pay into the Company Liquidation Dividend and Undistributed Assets Account any money representing unpaid dividends or undistributed assets in his hands at the date of dissolution.
- (3) **Furnishing of statement of all sums to Registrar with full particulars:** The liquidator shall, when making any payment referred to in sub-sections (1) and (2), furnish to the Registrar, a statement in the prescribed form, setting forth, in respect of all sums included in such payment,
- the nature of the sums,
 - the names and last known addresses of the persons entitled to participate therein,

- the amount to which each is entitled,
 - the nature of his claim thereto, and
 - such other particulars as may be prescribed.
- (4) **Entitlement of Liquidator to secure receipt from scheduled bank for any money paid:** The liquidator shall be entitled to a receipt from the scheduled bank for any money paid to it, and such receipt shall be an effectual discharge of the Company Liquidator in respect thereof.
- (5) **Procedure to be followed In case of voluntary winding up of company:** Where a company is being wound up voluntarily, the Company Liquidator shall, when filing a statement as per section 348,
- indicate the sum of money which is payable, during the six months preceding the date on which the said statement is prepared, and
shall, within 14 days of the date of filing the said statement;
 - pay that sum into the Company Liquidation Dividend and Undistributed Assets Account.
- (6) **Application to Registrar by a person claiming to be entitled to any money paid into Company Liquidation Dividend and Undistributed Assets Account:** Any person claiming to be entitled to any money paid into the Company Liquidation Dividend and Undistributed Assets Account, whether paid in pursuance of this section or under the provisions of any previous company law
- may apply to the Registrar for payment thereof, and
 - the Registrar, if satisfied that the person claiming is entitled, may make the payment to that person of the sum due.
- Period of settlement of claim:** Provided that the Registrar shall settle the claim of such person within a period of 60 days from the date of receipt of such claim, failing which the Registrar shall make a report to the Regional Director giving reasons of such failure.
- (7) **Transfer of unclaimed money paid into company Liquidation Dividend and Undistributed Assets Account to General Revenue account of CG:** Any money paid into the Company Liquidation Dividend and Undistributed Assets Account in pursuance of this section, which remains unclaimed thereafter -
- for a period of 15 years,
 - shall be transferred to the General Revenue Account of the Central Government,
 - but a claim to any money so transferred may be preferred under sub-section (6) and shall be dealt with as if such transfer had not been made and the order, if any, for payment on the claim will be treated as an order for refund of revenue.

(8) **Contravention by Liquidator:** Any liquidator retaining any money which should have been paid by him into the Company Liquidation Dividend and Undistributed Assets Account under this section shall—

- (a) **pay interest on the amount so retained at the rate of 12% per annum** and also pay such penalty as may be determined by the Registrar:

Provided that the Central Government may in any proper case remit either in part or in whole the amount of interest which the liquidator is required to pay under this clause;

- (b) **be liable to pay any expenses** occasioned by reason of his default; and
- (c) **where the winding up is by the Tribunal**, also be liable to have all or such part of his remuneration, as the Tribunal may consider just and proper, to be disallowed, and to be removed from his office by the Tribunal.

Example 5: A Ltd is getting wound up by the Tribunal u/s 271 of the Companies Act, 2013. Mr. P (Liquidator) had a sum of ₹ 45,00,000 which was deposited in Company Liquidation Dividend and Undistributed Assets Account. Mr. P was given a receipt of the same. Mr. X applied to the Registrar on 1st October, 2022 claiming ₹ 12,00,000 out of such amount. After verifying the correctness of the claim, the same was settled on 11th November, 2022. Balance amount remained unclaimed for a period of 15 years and hence was transferred to the General Revenue Account of the Central Government. It was noted that a sum of ₹ 6,00,000 was retained by Mr. P which should have been deposited by him into Company Liquidation Dividend and Undistributed Assets Account. Hence interest @ 15% p.a. was levied on Mr. P.

In the given case, Mr. X has made an application to the registrar for claiming ₹ 12,00,000 which is in accordance with the law. There is no need to submit any application to the Tribunal. The claim has been settled on 11th November, 2022 which is within 60 days from the date of receipt of the application (i.e. 1st October, 2022). The unclaimed amount has been transferred to the General Reserve Account of the Central Government after the amount has remained unclaimed for a period of 15 years which is also in accordance with the law. Interest levied @ 15% p.a. is in contravention of Section 352. Here interest @ 12% p.a. should be levied on Mr. P for his failure to deposit ₹ 6,00,000 into the Company Liquidation Dividend and Undistributed Assets Account.

Example 6: Mr. T is appointed as the Official Liquidator for carrying out the winding up process of FSM Ltd. The company has been declared wound up as on 01.06.2022. Rupees Two lakhs fifty thousand representing the amount unpaid to the creditors were not deposited into Company Liquidation Dividend and Undistributed Assets Account until 30.09.2022 by Mr. T. As per Section 352, the amount can be retained up to the period of six months. And since, six months had not elapsed in the above situation; no contravention is committed by Mr. T and so no action can be taken against him.

**52. LIQUIDATOR TO MAKE RETURNS, ETC. [SECTION 353]**

- (1) **Company Liquidator to make good the default within the specified time:** If any Company Liquidator who has made any default-
- in filing, delivering or making any return, account or other document, or
 - in giving any notice which he is by law required to file, deliver, make or give,
- fails to make good the default within 14 days after the service on him of a notice requiring him to do so, the Tribunal may, on an application made to it by any contributory or creditor of the company or by the Registrar, make an order directing the Company Liquidator to make good the default within such time as may be specified in the order.
- (2) **Cost to be borne by Company Liquidator:** Any order under sub-section (1) may provide that all costs of, and incidental to, the application shall be borne by the Company Liquidator.
- (3) **This section not to prejudice any other enactment imposing penalty on Company Liquidator:** Nothing in this section shall prejudice the operation of any enactment imposing penalties on a Company Liquidator in respect of any such default as aforesaid.

**53. MEETINGS TO ASCERTAIN WISHES OF CREDITORS OR CONTRIBUTORIES [SECTION 354]**

- (1) **Ascertainment of wishes of Creditors or Contributories:** In all matters relating to the winding up of a company, the Tribunal may—
- (a) **have regard to the wishes of creditors or contributories** of the company, as proved to it by any sufficient evidence;
 - (b) if it thinks fit for the purpose of ascertaining those wishes, **direct meetings of the creditors or contributories** to be called, held and conducted in such manner as the Tribunal may direct; and
 - (c) **appoint a person** to act as Chairman of any such meeting, and
 - (d) **to report the result** thereof to the Tribunal.
- (2) **While ascertaining the wishes of creditors,** regard shall be had to the value of each debt of the creditor.
- (3) **While ascertaining the wishes of contributories,** regard shall be had to the number of votes which may be cast by each contributory.



54. COURT, TRIBUNAL OR PERSON, ETC., BEFORE WHOM AFFIDAVIT MAY BE SWORN [SECTION 355]

- (1) **Court, Tribunal or Person before whom Affidavit may be sworn:** Any affidavit required to be sworn under the provisions, or for the purposes, of this Chapter may be sworn—
- in India before any court, Tribunal, judge or person lawfully authorised to take and receive affidavits; and
 - in any other country before any court, judge or person lawfully authorised to take and receive affidavits in that country or before an Indian diplomatic or consular officer.

Any affidavit required to be sworn under Chapter XX, may be sworn

in India, before

- any Court
- Tribunal
- Judge, or
- person lawfully authorised to take and receive affidavits;

in any other country, before

- any Court
- Judge or
- person lawfully authorised to take and receive affidavits
 - in that country or
 - before an Indian Diplomatic or Consular Officer

- (2) **Judicial notice of the seal, stamp or signature:** All Tribunals, Judges, Justices, Commissioners and persons acting judicially in India shall take judicial notice of the seal, stamp or signature, as the case may be, of any such Court, Tribunal, Judge, person, Diplomatic or Consular Officer, attached, appended or subscribed to any such affidavit or to any other document to be used for the purposes of this Chapter.



55. POWERS OF TRIBUNAL TO DECLARE DISSOLUTION OF COMPANY VOID [SECTION 356]

- (1) **Power of Tribunal to declare dissolution to be void at any time within two years:** Where a company has been dissolved, the Tribunal may -
- at any time within two years of the date of the dissolution,

- on application by the Company Liquidator of the company or
- by any other person who appears to the Tribunal to be interested,

make an order, upon such terms as the Tribunal thinks fit, declaring the dissolution to be void, and thereupon such proceedings may be taken as if the company had not been dissolved.

- (2) **Forwarding of certified copy of order of Tribunal with Registrar:** The Tribunal shall—
- (a) forward a copy of the order, within thirty days from the date thereof, to the Registrar who shall record the same; and
 - (b) direct the Company Liquidator or the person on whose application the order was made, to file a certified copy of the order, within thirty days from the date thereof or such further period as allowed by the Tribunal, with the Registrar who shall record the same.



56. COMMENCEMENT OF WINDING UP BY TRIBUNAL [SECTION 357]

The winding up of a company by the Tribunal under this Act shall be deemed to commence at the time of the presentation of the petition for the winding up.



57. EXCLUSION OF CERTAIN TIME IN COMPUTING PERIOD OF LIMITATION [SECTION 358]

Notwithstanding anything in the Limitation Act, 1963, or in any other law for the time being in force, in computing the period of limitation specified for any suit or application in the name and on behalf of a company which is being wound up by the Tribunal, the period from the date of commencement of the winding up of the company to a period of one year immediately following the date of the winding up order shall be excluded.

TEST YOUR KNOWLEDGE**Multiple Choice Questions**

1. A petition of winding up was filed against Raman Technology Ltd. under section 272 of the Companies Act, 2013. The Tribunal appointed a Company Liquidator and passed a winding up order on 20th of January 2023. As per the requirement of the Companies Act, 2013, state the correct statement with respect to submission of the Liquidator's report to the Tribunal:
 - (a) Liquidator shall submit its report to Tribunal within 30 days of its appointment by Tribunal.
 - (b) Liquidator shall submit its report to Tribunal within 45 days from winding up order.
 - (c) Liquidator shall submit its report to Tribunal within 60 days from winding up order.
 - (c) Liquidator shall submit its report to Tribunal within 90 days of its appointment by Tribunal.
2. The order for the winding up of a company shall operate in favour of:
 - (a) All contributories of the company
 - (b) All the creditors of the company
 - (c) All the contributories and the creditors of the company
 - (d) The Central/State Government
3. Mr. Raghav was appointed as Provisional Liquidator for X Ltd. against which an application for winding up was filed before the Tribunal. It is noteworthy that Mr. Raghav was having a shareholding in the same company. Enumerate the legal position of Mr. Raghav in the said condition in the light of the provisions related to its appointment in X Ltd. as per the Companies Act, 2013:
 - (a) Mr. Raghav cannot be appointed in X Ltd. because of having a shareholding in the same company.
 - (b) Mr. Raghav can be appointed in X Ltd. irrespective of his interest in the company because of his prior shareholding in the company before appointment.
 - (c) Mr. Raghav can be appointed in X Ltd. with the prior intimation to the Tribunal.
 - (d) Mr. Raghav can be appointed in X Ltd. by disclosing his shareholding by filing of declaration within 7 days from the date of his appointment by the Tribunal.
4. State, which amongst the following grounds, is incorrect for removal of the Provisional Liquidator or the Company Liquidator, as liquidator of the company:
 - (a) Independent working having no conflict of interest.

- (b) Professional incompetence or failure to exercise due care and diligence in performance of the powers and functions
 - (c) Misconduct
 - (d) Fraud or misfeasance
5. The Periodical reports made by the Company Liquidator to the Tribunal with respect to the progress of the winding up, to be submitted at the end of each, may be reviewed by on an application by
- (a) Quarter, Tribunal, Central Government
 - (b) Half Year, Tribunal, Company Liquidator
 - (c) Financial Year, Advisory Committee, Tribunal
 - (d) Quarter, Tribunal, Company Liquidator

Descriptive Questions

1. Info-tech Overtrading Ltd. was ordered to be wound up compulsory by an order dated 10th March, 2022 by the Tribunal. The official liquidator who had taken control of the assets and other records of the company had noticed the following:

The Managing Director of the company had sold certain properties belonging to the company to a private company in which his son was interested causing loss to the company to the extent of INR 50 lakhs. The sale took place on 15th October, 2021.

Examine what action the official liquidator can take in this matter, having regard to the provisions of the Companies Act, 2013.

2. XYZ Limited is being wound up by the Tribunal. All the assets of the company have been charged to the company's bankers to whom the company owes ₹ 5 crores. The company owes following amounts to others:

- Dues to workers – ₹ 1,25,00,000
- Taxes Payable to Government – ₹ 30,00,000
- Unsecured Creditors – ₹ 60,00,000

You are required to compute with the reference to the provisions of the Companies Act, 2013 the amount each kind of creditors is likely to get if the amount realized by the official liquidator from the sale of secured assets and available for distribution among creditors is only ₹ 4,00,00,000/-.

3. *Suman Info-tech Ltd. was ordered to be compulsory wound up by an order dated 10th March, 2022 by the Tribunal. The official liquidator who had taken control of the assets and other records of the company had noticed that:*

- (i) *One of the contributories whose calls were pending to be paid is about to leave India to evade payment of calls and;*
- (ii) *A person having books of accounts of the company in his possession might abscond to avoid examination of books of account in respect of the affairs of the company.*

Apprehending such possibilities, Tribunal detained such contributory for next 6 months disallowing him to leave India as well as arrested and seized books of account from the person who might possibly abscond to avoid examination of the affairs of the company.

Referring to the provisions of Companies Act, 2013, answer the following in the current scenario:

- (i) *What is the validity of Tribunal's order for detention of contributory disallowing him to leave India?*
 - (ii) *Is it correct on Tribunal's part to arrest and seize books of accounts from the person planning to abscond to avoid examination of books of accounts in respect of the affairs of the company?*
4. *Due to an unprecedented flood, all the fixed assets of a Company were damaged extensively beyond renovation or repair. The costs of replacement of assets were huge and the sum insured on the fixed assets did not cover all the assets. Therefore, the operations of the Company were permanently discontinued. Meanwhile, based on a winding-up petition filed by the secured creditors, the High Court passed a winding-up order. The workers of the Company opposed the winding-up petition and also filed an appeal against the winding-up order. The workers were not sure whether their appeal would be heard in the winding-up proceedings. Examine, under the provisions of the Companies Act, 2013, whether the appeal filed by the workers would succeed and their dues / interest will be protected in priority?*
5. *Clarks Clocks Limited, has made default in filing financial statements and annual returns for a continuous period of four financial years ending on 31st March, 2022. The Registrar of Companies having jurisdiction approached the Central Government to accord sanction to present a petition to Tribunal (NCLT) for the winding up of the company in accordance with the above ground under Section 272 of the Companies Act, 2013.*
- Examine the validity of the action of ROC, keeping in view the relevant provisions of the Companies Act, 2013. State the time limit for passing an order by the Tribunal under Section 273 of the Companies Act, 2013?*

ANSWERS**Answer to Multiple Choice Questions**

1.	c	2.	c	3.	d	4.	a	5.	d

Answer to Descriptive Questions

1. The official liquidator can invoke the provisions contained in Section 328 of the Companies Act, 2013 to recover the assets of the company so sold. According to Section 328, if the Tribunal is satisfied that there is a preference transfer of property, movable or immovable, or any delivery of goods, payment, execution made, taken or done by or against a company within six months before making winding up application, the Tribunal may order as it may think fit and may declare such transaction invalid and restore the position.

Since in the present case, the sale of immovable property took place on 15th October, 2021 and the company went into liquidation on 10th March, 2022 *i.e.*, within 6 months before the winding up of the company and since the sale has resulted in a loss of INR 50 lakhs to the company.

The official liquidator will be able to succeed in proving the case under Section 328 by way of fraudulent preference as the property was sold to a private company in which the son of the Managing Director was interested.

Hence, the transaction made will be regarded as invalid and the position will be restored as if no transfer of immovable property had been made.

2. Section 326 of the Companies Act, 2013 talks about the overriding preferential payments to be made from the amount realized from the assets to be distributed to various kind of creditors. According to the proviso given in section 326 the security of every secured creditor shall be deemed to be subject to a *pari passu* charge in favour of the workmen to the extent of their portion.

$$\text{Workmen's Share to Secured Assets} = \frac{\text{Amount Realised} * \text{Workmen's Dues}}{\text{Workmen's Dues} + \text{Secured Loan}}$$

$$\text{Workmen's Share to Secured Assets} = \frac{4,00,00,000 * 1,25,00,000}{1,25,00,000 + 5,00,00,000}$$

$$4,00,00,000 * \frac{1}{5}$$

$$\text{Workmen's Share to Secured Assets} = 80,00,000$$

Amount available to secured creditor is ₹ 400 Lakhs – 80 Lakhs = 320 Lakhs

Hence, no amount is available for payment of government dues and unsecured creditors.

3. According to Section 301 of the Companies Act, 2013, at any time either before or after passing a winding up order, if the Tribunal is satisfied that

- a contributory or
- a person having property, accounts or papers of the company in his possession

is about to leave India or otherwise to abscond, or is about to remove or conceal any of his property, for the purpose of evading payment of calls or of avoiding examination respecting the affairs of the company,

the Tribunal may cause—

- (a) the contributory to be detained until such time as the Tribunal may order; and
- (b) his books and papers and movable property to be seized and safely kept until such time as the Tribunal may order.

In the instant case, by considering the above provisions:

- (i) The Tribunal's order for detention of contributory for next 6 months disallowing him to leave India, is valid.
- (ii) It is correct on the part of Tribunal to arrest and seize books of accounts from the person planning to abscond to avoid examination of books of accounts in respect of the affairs of the company.

4. According to section 279 of the Companies Act, 2013, when a winding up order has been passed or a provisional liquidator has been appointed, no suit or other legal proceeding shall be commenced, or if pending at the date of the winding up order, shall be proceeded with, by or against the company, except with the leave of the Tribunal and subject to such terms as the Tribunal may impose.

It is further provided that any application to the Tribunal seeking leave under this section shall be disposed of by the Tribunal within sixty days.

However, the above provision shall not apply to any proceeding pending in appeal before the Supreme Court or a High Court.

According to section 325/326/327 of the Companies Act, 2013, in the winding up of a company under this Act, the workmen's dues shall be paid in priority to all other debts ranking *pari passu* with secured creditors.

As per the facts of the case, the High Court has already passed a winding up order of the company. Hence, the workmen can appeal against the winding up order but only with the leave of the Tribunal and subject to such terms as the Tribunal may impose. Further, the dues/ interest of the workmen will be protected in priority as workmen's dues shall be paid in priority to all other debts ranking *pari passu* with secured creditors.

5. **Validity of ROC's action:** According to Section 271(d) of the Companies Act, 2013, a Company may, on a petition under Section 272, be wound up by the Tribunal, if the Company has made a default in filing with the Registrar its financial statements or annual returns for immediately preceding five consecutive financial years.

In the instant case, the move by RoC to present a petition to Tribunal for the winding up of Clarks Clocks Limited is not valid as the Company has made default in filing financial statements and annual returns for a continuous period of four financial years ending on 31st March, 2022.

Time limit for passing of an Order under section 273: An order under section 273 of the Act shall be made within ninety days from the date of presentation of the petition.

[illegible]

CHAPTER

8

MISCELLANEOUS PROVISIONS



LEARNING OUTCOMES

After reading this chapter, you will be able to:

- ☐ Know the provisions of Registered Valuers and Valuation Rules.
- ☐ Know the provisions regarding Removal of names of companies from the Register of Companies.
- ☐ Identify the Government companies and their Annual Reports.
- ☐ Analyzing the concept of Nidhis and Dormant companies.
- ☐ Know about Miscellaneous Provisions.



1. INTRODUCTION

Ministry of Corporate Affairs vide Notifications dated 7th of December & 26th of December, 2016 notified various sections of the Companies Act, 2013. Besides, with the enforcement of the Insolvency and Bankruptcy Code, 2016, many substantial changes have also made in the Companies Act, 2013.



2. REGISTERED VALUER

Provisions related to the Registered Valuers are dealt under Section 247 read with the Companies (Registered Valuers and Valuation) Rules, 2017 of The Companies Act, 2013. Sections deals with what all property can be valued and by whom as per the prescribed term and conditions, role of the Registered Valuers and the consequences of contravention in the legal compliance by the valuer.

(i) **Nature of the assets for Valuation:** Valuation is required to be made in respect of any

- property,
- stocks,
- shares,
- debentures,
- securities,
- goodwill,
- any other assets (herein referred to as the assets) or
- net worth of a company or its liabilities under the provision of this Act.

Appointment of valuer: A Registered Vauer shall be appointed by a person having such qualifications and experience, registered as a valuer and being a member of an organisation recognised, in such manner, on such terms and conditions as may be prescribed and appointed by the audit committee or in its absence by the Board of Directors of that company.

(ii) **Role of Valuer:** The valuer appointed under sub-section (1) shall,—

- (a) make an **impartial, true and fair valuation of any assets** which may be required to be valued;
- (b) **exercise due diligence** while performing the functions as valuer;
- (c) make the **valuation in accordance with such rules** as may be prescribed; and
- (d) **not undertake valuation of any assets in which he has a direct or indirect interest** or becomes so interested at any time during a period of three years prior to his appointment as valuer or three years after the valuation of assets was conducted by him.

- (iii) **Contravention:** If a valuer contravenes the provisions of this section or the rules made thereunder, the valuer shall be liable to a penalty of fifty thousand rupees. However, if the valuer has contravened such provisions with the intention to defraud the company or its members, he shall be punishable with imprisonment for a term which may extend to 1 year and with fine which shall not be less than ₹ 1 Lakh but which may extend to ₹ 5 lakhs.
- (iv) **Levying penalties:** Where a valuer has been convicted under point (iii) above, he shall be liable to—
 - (a) **refund the remuneration** received by him to the company; and
 - (b) **pay for damages** to the company or to any other person for loss arising out of incorrect or misleading statements of particulars made in his report.

COMPANIES (REGISTERED VALUERS AND VALUATION) RULES, 2017

These rules shall apply for valuation in respect of any property, stocks, shares, debentures, securities or goodwill or any other assets or net worth of a company or its liabilities under the provision of the Act or these rules.

Explanation.- It is hereby clarified that conduct of valuation under any other law other than the Act or these rules by any person shall not be affected by virtue of coming into effect of these rules.

Rule 2: Definitions

1. In these rules, unless the context otherwise requires —
 - (a) **“Act”** means the Companies Act, 2013 (18 of 2013);
 - (b) **“authority”** means an authority specified by the Central Government under section 458 of the Companies Act, 2013 to perform the functions under these rules;
 - (c) **“asset class”** means a distinct group of assets, such as land and building, machinery and equipment, displaying similar characteristics, that can be classified and requires separate set of valuers for valuation;
 - (d) **“certificate of recognition”** means the certificate of recognition granted to a registered valuers organisation under sub-rule (5) of rule 13 and the term “recognition” shall be construed accordingly;
 - (e) **“certificate of registration”** means the certificate of registration granted to a valuer under sub-rule (6) of rule 6 and the term “registration” shall be construed accordingly;
 - (f) **“partnership entity”** means a partnership firm registered under the Indian Partnership Act, 1932 (9 of 1932) or a limited liability partnership registered under the Limited Liability Partnership Act, 2008 (6 of 2009);
 - (g) **“Annexure”** means an annexure to these rules;

- (h) **"registered valuers organisation"** means a registered valuers organization recognised under sub-rule (5) of rule 13;
- (i) **"valuation standards"** means the standards on valuation referred to in rule 18; and
- (j) **"valuer"** means a person registered with the authority in accordance with these rules and the term "registered valuer" shall be construed accordingly.

Rule 3: Eligibility for registered valuers

- (1) A person shall be **eligible to be a registered valuer if he-**
 - (a) is a **valuer member** of a registered valuers organisation;
Explanation— For the purposes of this clause, "a valuer member" is a member of a registered valuers organisation who possesses the requisite educational qualifications and experience for being registered as a valuer;
 - (b) is **recommended by the registered valuers organisation** of which he is a valuer member for registration as a valuer;
 - (c) has **passed the valuation examination** under rule 5 **within three years** preceding the date of making an application for registration under rule 6;
 - (d) possesses the **qualifications and experience** as specified in rule 4;
 - (e) is **not a minor**;
 - (f) has **not been declared to be of unsound mind**;
 - (g) is **not an undischarged bankrupt**, or has not applied to be adjudicated as a bankrupt;
 - (h) is a **person resident in India**;
Explanation— For the purposes of these rules 'person resident in India' shall have the same meaning as defined in clause (v) of section 2 of the Foreign Exchange Management Act, 1999 as far as it is applicable to an individual;
 - (i) has **not been convicted** by any competent court for an offence punishable with imprisonment for a term exceeding 6 months or for an offence involving moral turpitude, and a period of 5 years has not elapsed from the date of expiry of the sentence;
Provided that if a person has been convicted of any offence and sentenced in respect thereof to imprisonment for a period of 7 years or more, he shall not be eligible to be registered;
 - (j) has **not been levied a penalty** under section 271J of Income-tax Act, 1961 and time limit for filing appeal before Commissioner of Income-tax (Appeals) or

Income-tax Appellate Tribunal, as the case may be has expired, or such penalty has been confirmed by Income-tax Appellate Tribunal, and 5 years have not elapsed after levy of such penalty; and

(k) is a fit and proper person;

Explanation— For determining whether an individual is a fit and proper person under these rules, the authority may take account of any relevant consideration, including but not limited to the following criteria-

- (i) integrity, reputation and character,
- (ii) absence of convictions and restraint orders, and
- (iii) competence and financial solvency.

(2) **No partnership entity or company shall be eligible to be a registered valuer if-**

- (a) it has been set up for objects other than for rendering professional or financial services, including valuation services and that in the case of a company, it is a subsidiary, joint venture or associate of another company or body corporate;
- (b) it is undergoing an insolvency resolution or is an undischarged bankrupt;
- (c) all the partners or directors, as the case may be, are not eligible under clauses (c), (d), (e), (f), (g), (h), (i), (j) and (k) of sub-rule (1);
- (d) 3 or all the partners or directors, whichever is lower, of the partnership entity or company, as the case may be, are not registered valuers; or
- (e) none of its partners or directors, as the case may be, is a registered valuer for the asset class, for the valuation of which it seeks to be a registered valuer.
- (f) it is not a member of register valuers organisation: Provided that it shall not be a member of more than one such register valuers organization at a given point of time; provided further that the partnership entity or company, already registered as valuers, on the date of commencement of the Companies (Register Valuers and Valuation) Amendment Rules, 2022, shall comply within six months of such commencement with the conditions specified under this clause.

Example 1: The Board of Directors of Tim Tim Ltd. proposes to appoint Mr. Nirala, an individual as the valuer for carrying out valuation of an immovable property as required under the provisions of the Companies Act, 2013. The approval of Audit Committee was not taken for such appointment.

In the given case, as there is audit committee in the company, Board of Director does not have right to appoint the valuer. It is against the said provision. In fact, valuer proposes to be appointed shall have such qualification and experience and registered as a valuer in such

manner, on such terms and conditions as may be prescribed and appointed by the audit committee or in its absence by the Board of Directors of that company.

Sagar Dattatray Goge., In re, IBBI/VALUATION/DISC./3/2021, FEBRUARY 9, 2021, it was ordered that ,where 'G' was granted registration as valuer by IBBI but 'G' concealed information of pendency of criminal proceedings against him, registration of 'G' as Registered Valuer was to be cancelled for violation of rule 3 of Companies (Registered Valuers and Valuation) Rules, 2017.

Rule 4: Qualifications and experience

An individual shall have the following qualifications and experience to be eligible for registration under rule 3, namely:-

- (a) **post-graduate degree or post-graduate diploma**, in the specified discipline, from a University or Institute established, recognised or incorporated by law in India and at least three years of experience in the specified discipline thereafter; or
- (b) **a Bachelor's degree or equivalent**, in the specified discipline, from a University or Institute established, recognised or incorporated by law in India and at least five years of experience in the specified discipline thereafter; or
- (c) **membership of a professional institute** established by an Act of Parliament enacted for the purpose of regulation of a profession with at least three years' experience after such membership.

Explanation- For the purposes of this clause the 'specified discipline' shall mean the specific discipline which is relevant for valuation of an asset class for which the registration as a valuer or recognition as a registered valuers organisation is sought under these rules.

Rule 5: Valuation Examination

- (1) **Conduct of Examination:** The authority shall, either on its own or through a designated agency, conduct valuation examination for one or more asset classes, for individuals, qualifications and experience as specified in rule 4, and have completed their educational courses as member of a registered valuers organisation, to knowledge, skills, values and ethics in respect of valuation:

Provided that the authority may recognise an educational course conducted by a registered valuers organisation before its recognition as adequate appearing for valuation examination:

Provided also that the authority may recognise an examination conducted as part of a master's or post graduate degree course conducted by equivalent to the valuation examination.

- (2) **Determination of Syllabus:** The authority shall determine the syllabus for various valuation specific subjects or assets classes for the valuation examination on the recommendation Committee of experts constituted by the authority in this regard.

- (3) **Publishing details on the website:** The syllabus, format and frequency of the valuation examination, including qualifying marks, shall be published on the website of the authority at least the examination.
- (4) **Acknowledgment of passing examination:** An individual who passes the valuation examination, shall receive acknowledgement of passing the examination.
- (5) **Number of attempts:** An individual may appear for the valuation examination any number of times.

Rule 6: Application for certificate of registration

1. **Manner of applying for registration:** In the following manner an application can be applied for obtaining of certificate of registration from following class of person who are eligible for registration as a registered valuer under rule 3:

Class	Application filing
An individual	make an application to the authority in Form A of Annexure-II along with a non-refundable application fee of five thousand rupees in favour of the authority
A partnership entity or company	may make an application to the authority in Form-B of Annexure-II along with a non-refundable application fee of ten thousand rupees in favour of the authority

Examination of application: The authority shall examine the application, and may grant twenty one days to the applicant to remove the deficiencies, if any, in the application.

Submission of documents: The authority may require the applicant to submit additional documents or clarification within twenty- one days.

Appearance of applicant before the authority: The authority may require the applicant to appear, within twenty one days, before the authority in person, or through its authorised representative for explanation or clarifications required for processing the application.

Grant of certificate: If the authority is satisfied, after such scrutiny, inspection or inquiry as it deems necessary, that the applicant is eligible under these rules, it may grant a certificate of registration to the applicant to carry on the activities of a registered valuer for the relevant asset class or classes in **Form-C** of the **Annexure-II** within sixty days of receipt of the application, excluding the time given by the authority for presenting additional documents, information or clarification, or appearing in person, as the case may be.

In case of denial of registration: If, after considering an application made under this rule, the authority is of the *prima facie* opinion that the registration ought not be granted, it shall communicate the reasons for forming such an opinion within forty-five days of receipt of the

application, excluding the time given by it for removing the deficiencies, presenting additional documents or clarifications, or appearing in person, as the case may be.

Call for an explanation: The applicant shall submit an explanation as to why his/its application should be accepted within fifteen days of the receipt of the communication to enable the authority to form a final opinion.

Consideration by authority: After considering the explanation, if any, given by the applicant, the authority shall either -

- (a) accept the application and grant the certificate of registration; or
- (b) reject the application by an order, giving reasons thereof.

The authority shall communicate its decision to the applicant within thirty days of receipt of explanation.

Rule 7: Conditions of Registration

The registration granted under rule 6 shall be **subject to the conditions** that the valuer shall -

- (a) at all times possess the eligibility and qualification and experience criteria as specified under rule 3 and rule 4;
- (b) at all times comply with the provisions of the Act, these rules and the Bye-laws or internal regulations, as the case may be, of the respective registered valuers organisation;
- (c) in his capacity as a registered valuer, not conduct valuation of the assets or class(es) of assets other than for which he/it has been registered by the authority;
- (d) take prior permission of the authority for shifting his/ its membership from one registered valuers organisation to another;
- (e) take adequate steps for redressal of grievances;
- (f) maintain records of each assignment undertaken by him for at least three years from the completion of such assignment;
- (g) comply with the Code of Conduct of the registered valuers organisation of which he is a member;
- (h) in case a partnership entity or company is the registered valuer, allow only the partner or director who is a registered valuer for the asset class(es) that is being valued to sign and act on behalf of it;
- (i) in case a partnership entity or company is the registered valuer, it shall disclose to the company concerned, the extent of capital employed or contributed in the partnership

entity or the company by the partner or director, as the case may be, who would sign and act in respect of relevant valuation assignment for the company;

- (j) in case a partnership entity is the registered valuer, be liable jointly and severally along with the partner who signs and acts in respect of a valuation assignment on behalf of the partnership entity;
- (k) in case a company is the registered valuer, be liable along with director who signs and acts in respect of a valuation assignment on behalf of the company;
- (l) in case a partnership entity or company is the registered valuer, immediately inform the authority on the removal of a partner or director, as the case may be, who is a registered valuer along with detailed reasons for such removal; and
- (m) comply with such other conditions as may be imposed by the authority.

Rule 7A: Intimation of changes in personal details etc., by register valuer to authority-

A register valuer shall intimate the authority for change in the personal details, or any modification in the composition of partners or directors, or any modification in any clause of the partnership agreement or memorandum of association, which may affect registration of register valuer, after paying fee as per the Table-I in **Annexure V**.

Rule 8: Conduct of Valuation

- (1) The registered valuer shall, while conducting a valuation, comply with the valuation standards as notified or modified under rule 18:

Provided that until the valuation standards are notified or modified by the Central Government, a valuer shall make valuations as per-

- (a) Internationally accepted valuation standards; or
 - (b) Valuation standards adopted by any registered valuers organisation.
- (2) The registered valuer may obtain inputs for his valuation report or get a separate valuation for an asset class conducted from another registered valuer, in which case he shall fully disclose the details of the inputs and the particulars etc. of the other registered valuer in his report and the liabilities against the resultant valuation, irrespective of the nature of inputs or valuation by the other registered valuer, shall remain of the first mentioned registered valuer.
 - (3) The valuer shall, in his report, state the following:-
 - (a) Background information of the asset being valued;
 - (b) Purpose of valuation and appointing authority;
 - (c) Identity of the valuer and any other experts involved in the valuation;

- (d) Disclosure of valuer interest or conflict, if any;
- (e) Date of appointment, valuation date and date of report;
- (f) Inspections and/or investigations undertaken;
- (g) Nature and sources of the information used or relied upon;
- (h) Procedures adopted in carrying out the valuation and valuation standards followed;
- (i) Restrictions on use of the report, if any;
- (j) Major factors that were taken into account during the valuation;
- (k) Conclusion; and
- (l) Caveats, limitations and disclaimers to the extent they explain or elucidate the limitations faced by valuer, which shall not be for the purpose of limiting his responsibility for the valuation report.

Rule 9: Temporary surrender

- (1) A registered valuer may temporarily surrender his registration certificate in accordance **with the bye-laws or regulations**, as the case may be, of the registered valuers organisation and on such surrender, the valuer shall inform the authority for taking such information on record.
- (2) A registered valuers organisation shall **inform the authority if any valuer member has temporarily surrendered his/its membership** or revived his/ its membership after temporary surrender, not later than seven days from approval of the application for temporary surrender or revival, as the case may be.
- (3) Every registered valuers organisation shall **place, on its website**, in a searchable format, the names and other details of its valuers members who have surrendered or revived their memberships.

Rule 12: Eligibility for registered valuers organisation

- (1) An organisation that meets requirements under sub-rule (2) may be recognised as a registered valuers organisation for valuation of a specific asset class or asset classes if —
 - (i) it has been registered under section 25 of the Companies Act, 1956 or section 8 of the Companies Act, 2013 with the sole object of dealing with matters relating to regulation of valuers of an asset class or asset classes and has in its bye laws the requirements specified in **Annexure-III**;

- (ii) it is a professional institute established by an Act of Parliament enacted for the purpose of regulation of a profession;

Provided that, subject to sub-rule (3), the following organisations may also be recognised as a registered valuers organisation for valuation of a specific asset class or asset classes, namely:-

- (a) an organisation registered as a society under the Societies Registration Act, 1860 or any relevant state law, or;
 - (b) an organisation set up as a trust governed by the Indian Trust Act, 1882.
- (2) The organisation referred to in sub-rule (1) shall be recognised if it –
- (a) conducts educational courses in valuation, in accordance with the syllabus determined by the authority, under rule 5, for individuals who may be its valuers members, and delivered in class room or through distance education modules and which includes practical training;
 - (b) grants membership or certificate of practice to individuals, who possess the qualifications and experience as specified in rule 4, in respect of valuation of asset class for which it is recognised as a registered valuers organisation;
 - (c) conducts training for the individual members before a certificate of practice is issued to them;
 - (d) lays down and enforces a code of conduct for valuers who are its members, which includes all the provisions specified in **Annexure-I**;
 - (e) provides for continuing education of individuals who are its members;
 - (f) monitors and reviews the functioning, including quality of service, of valuers who are its members; and
 - (g) has a mechanism to address grievances and conduct disciplinary proceedings against valuers who are its members.
- (3) A registered valuers organisation, being an entity under proviso to sub-rule (1), shall convert into or register itself as a company under section 8 of the Companies Act, 2013, and include in its bye laws the requirements specified in **Annexure- III**, within one year from the date of commencement of these rules.

Rule 16: Complaint against a registered valuer or registered valuers organisation

A complaint may be filed against a registered valuer or registered valuers organisation before the authority in person or by post or courier along with a non-refundable fees of ₹ 1,000 in favour of the authority and the authority shall examine the complaint and take such necessary action as it deems fit:

Provided that in case of a complaint against a registered valuer, who is a partner of a partnership entity or director of a company, the authority may refer the complaint to the relevant registered valuers organisation and such organisation shall handle the complaint in accordance with its bye laws.

Rule 18: Valuation Standards

The Central Government shall notify and may modify (from time to time) the valuation standards on the recommendations of the Committee set up under rule 19.

Composition of the committee as per Rule 19:

- 1 Chairperson (well versed in valuation, finance, accountancy etc.);
- 1 member nominated by Ministry of Corporate Affairs;
- 1 member nominated by Insolvency and Bankruptcy Board of India;
- 1 member nominated by legislative department;
- Upto 4 members, nominated by Central Government representing authorities which are allowing valuations by registered valuers;
- Upto 4 members, representatives of registered valuer organization, nominated by Central Government;
- Upto 2 members to represent industry and other stakeholders nominated by the Central Government in consultation with the authority;
- President of ICAI, ICSI, Institute of Cost Accountants of India as ex-officio members

Chairperson and members of committee shall have a tenure of 3 years & maximum 2 tenures.

Rule 20: Punishment for contravention

Without prejudice to any other liabilities where a person contravenes any of the provision of these rules he shall be punishable in accordance with sub-section (3) of section 469 of the Act.

Rule 21: Punishment for false statement

If in any report, certificate or other document required by, or for, the purposes of any of the provisions of the Act or the rules made thereunder or these rules, any person makes a statement,—

- (a) which is false in any material particulars, knowing it to be false; or
- (b) which omits any material fact, knowing it to be material, he shall be liable under section 448 of the Act.

Example 2: Mr. Bhola director of Bhandari Ltd. entered into an arrangement with his friend and acquired asset on the name of Bhandari Ltd. by passing resolution in the general meeting

of the company. The notice for approval of resolution by the company included the particulars of the arrangement along with the value of the asset duly calculated by a registered valuer. Later, the Board of company discovered the loss arising out of incorrect statement in the report made by the valuer.

In this case, valuer is liable to be convicted for the incorrect statement given in the report made with an intent to defraud the company or its members.



3. REMOVAL OF NAMES OF COMPANIES FROM THE REGISTER OF COMPANIES

Provision related to removal of names of companies from the register of companies is covered in Chapter XVIII of the Companies Act, 2013. This chapter comprises of five sections being covered from Section 248 to 252.

[I] **Power of Registrar to Remove Name of Company from Register of Companies [Section 248]**

(1) **Power of registrar:** Where the Registrar has reasonable cause to believe that—

- (a) a company has **failed to commence its business within one year** of its incorporation, or;
- (b) omitted
- (c) a company is **not carrying on any business or operation for a period of two immediately preceding financial years** and has **not made any application within such period for obtaining the status of a dormant company** under section 455, or;
- (d) the **subscribers to the memorandum have not paid the subscription** which they had undertaken to pay at the time of incorporation of a company **and a declaration to this effect has not been filed within one hundred and eighty days** of its incorporation under sub-section (1) of section 10A; or
- (e) the company is **not carrying on any business or operations, as revealed after the physical verification** carried out under sub-section (9) of section 12,

he shall **send a notice** to the company and all the directors of the company, of his intention to remove the name of the company from the register of companies and requesting them to send their representations along with copies of the relevant documents, if any, within a period of thirty days from the date of the notice.

(2) **Filing of application to registrar by company for removal of name:** A company may, after extinguishing all its liabilities, by-

- a special resolution, or

- consent of seventy-five per cent. members in terms of paid-up share capital,

file an application in the prescribed manner to the Registrar for removing the name of the company from the register of companies on all or any of the grounds specified in sub-section (1) and the Registrar shall, on receipt of such application, cause a public notice to be issued in the prescribed manner:

Approval of the regulatory body, in case of a company regulated under a special Act:

Provided that in the case of a company regulated under a special Act, approval of the regulatory body constituted or established under that Act shall also be obtained and enclosed with the application.

- (3) **Exemption to section 8 companies:** Nothing in sub-section (2) shall apply to a company registered under section 8.
- (4) **Publishing of notice for general public:** A notice issued under sub-section (1) or sub-section (2) shall be published in the prescribed manner and also in the Official Gazette for the information of the general public.
- (5) **Strike off of names from register of companies:** At the expiry of the time mentioned in the notice, the Registrar may, unless cause to the contrary is shown by the company, strike off its name from the register of companies, and shall publish notice thereof in the Official Gazette, and on the publication in the Official Gazette of this notice, the company shall stand dissolved.
- (6) **Provisions for realisation of amount:** The Registrar, before passing an order under sub-section (5), shall satisfy himself that sufficient provision has been made for the realisation of all amount due to the company and for the payment or discharge of its liabilities and obligations by the company within a reasonable time and, if necessary, obtain necessary undertakings from the managing director, director or other persons in charge of the management of the company:

Provided that notwithstanding the undertakings referred to in this sub-section, the assets of the company shall be made available for the payment or discharge of all its liabilities and obligations even after the date of the order removing the name of the company from the register of companies.
- (7) **Existence of the liability:** The liability, if any, of every director, manager or other officer who was exercising any power of management, and of every member of the company dissolved under sub-section (5), shall continue and may be enforced as if the company had not been dissolved.
- (8) **Not affecting on the power of tribunal:** Nothing in this section shall affect the power of the Tribunal to wind up a company the name of which has been struck off from the register of companies.

Example 3: The Registrar of Companies (ROC) was reviewing the financial statements of White Steam Pvt. Ltd which was incorporated 8 months ago. The ROC found that the subscribers to the Memorandum of Association of the company had not paid the subscription money nor had they filed a declaration to this effect. ROC strike off the name of the company from the register of companies. In this case there is non-compliance.

As per Section 248 (1)(b) of the Companies Act, where the Registrar has reasonable cause to believe that— the subscribers to the memorandum have not paid the subscription which they had undertaken to pay within a period of one hundred and eighty days from the date of incorporation of a company and a declaration under sub-section (1) of section 11 to this effect has not been filed within one hundred and eighty days of its incorporation; he shall send a notice to the company and all the directors of the company, of his intention to remove the name of the company from the register of companies and requesting them to send their representations along with copies of the relevant documents, if any, within a period of thirty days from the date of the notice.

Since the subscribers have not paid the subscription money within 180 days of incorporation, the ROC shall send to the Company a notice stating his intention to remove the name of the company from the Register of Companies and requesting them to send their representations within 30 days from date of notice. Such notice was not send by ROC to the company.

Example 4: ABC Life Insurance Company Ltd. was incorporated following all the legal procedures but the company cannot commence its operation for a period of one year since its incorporation. The members decided to get its name removed from the Registrar of Companies. Consent of eighty percent members in terms of paid-up share capital was taken for the removal of name. Thus, an application was filed for this purpose. Application is said to be invalid, as the approval of IRDA must be obtained first. As per Section 248(2), when a company is regulated as per a Special Act, the approval the regulatory authority is needed and should be enclosed with the application for removal of name.

1. In *HIFFCO Farming Ltd. v. Registrar of Companies*, Company Appeal (AT) No. 51 of 2022, April 21, 2022, it was held that where appellant company had not filed financial statement with Registrar of Companies from year 2006-07 onwards and its name was 'struck-off' from Register of Companies, in view of fact that company was carrying on business operation and right to seek restoration of name of company was not extinguished, name of company was to be restored in register of companies subject to filing of all pending statutory documents along with late fees.

2. In *Nirendra Nath Kar v. Gopal Navin Bhai Dave*, Civil Appeal No. 4448 of 2015, September 29, 2022, it was decided that where an application for restoration of company was made by one who was neither company nor a member nor a creditor, he could not be said to be a person aggrieved to question order of RoC striking off name of company from Register of Companies and, thus, he had no locus standi to file application for restoration of name of company

[II] Restrictions on making application under section 248 in certain situations [Section 249]

- (1) An application under section 248 on behalf of a company shall not be made if, at any time in the previous three months, the company—
 - (a) has changed its name or shifted its registered office from one State to another;
 - (b) has made a disposal for value of property or rights held by it, immediately before cesser of trade or otherwise carrying on of business, for the purpose of disposal for gain in the normal course of trading or otherwise carrying on of business;
 - (c) has engaged in any other activity except the one which is necessary or expedient for the purpose of making an application under that section, or deciding whether to do so or concluding the affairs of the company, or complying with any statutory requirement;
 - (d) has made an application to the Tribunal for the sanctioning of a compromise or arrangement and the matter has not been finally concluded; or
 - (e) is being wound up under Chapter XX of this Act or under the Insolvency and Bankruptcy Code, 2016.
- (2) **Violation of above conditions on filing of application:** If a company files an application in violation of restriction as given in sub-section (1) as given above, it shall be punishable with fine which may extend to one lakh rupees.
- (3) **Rights of registrar on non-compliance of conditions by the company:** An application filed under sub-section (2) of section 248 shall be withdrawn by the company or rejected by the Registrar as soon as conditions under sub-section (1) are brought to his notice.

Application under section 248 is restricted, if at any time in the previous three months, the company-

- changed its name or shifted its registered office
- made a disposal for value of property or rights held by it
- engaged in any other activity except the one which is necessary or expedient
- made an application to the Tribunal for the sanctioning of a compromise or arrangement
- wound up

Example 5: A-Com is a private limited company incorporated in the year 2013. The company deals in manufacturing of glasses. Since May 2018, the company is not carrying any business operations. In April 2020, the company shifted its registered office from Jaipur to Ahmedabad. On 2nd May 2020, Company decided to file an application for Strike off. According to section 249, the said act of the company will not be valid because application can be filed only after 3 months from the date the company shifted its registered office.

[III] Effect of Company Notified as Dissolved [Section 250]

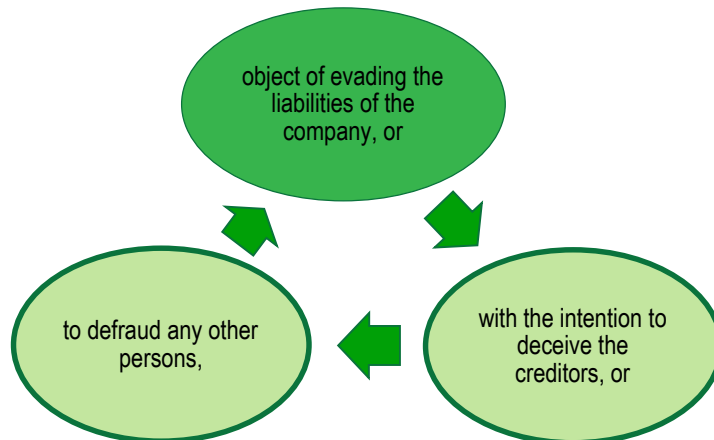
Where a company stands dissolved under section 248, it shall on and from the date mentioned in the notice –

- cease to operate as a company, and
- the Certificate of Incorporation issued to it shall be deemed to have been cancelled from such date.

For the purpose of realising the amount due to the company and for the payment or discharge of the liabilities or obligations of the company, this sub-section shall not effect. The company shall be continued in existence.

[IV] Fraudulent Application for Removal of Name [Section 251]

- (1) **Intention of filing application:** Where it is found that an application by a company has been made with the-



the persons in charge of the management of the company shall, notwithstanding that the company has been notified as dissolved—

- (a) be **jointly and severally liable** to any person or persons who had incurred loss or damage as a result of the company being notified as dissolved; and
 - (b) be **punishable for fraud** in the manner as provided in section 447.
- (2) **Recommendation for prosecution:** The Registrar may also recommend prosecution of the persons responsible for the filing of an application.

[V] Appeal to Tribunal [Section 252]

- (1) **Aggrieved person to file an appeal against the order of registrar:** Any person aggrieved by an order of the Registrar, notifying a company as dissolved under section 248, may file an appeal to the Tribunal within a period of three years from the date of the order of the Registrar and if the Tribunal is of the opinion that the removal of the name of the company from the

register of companies is not justified in view of the absence of any of the grounds on which the order was passed by the Registrar, it may order restoration of the name of the company in the register of companies.

Reasonable opportunity of representations given to registrar: Before passing any order under this section, the Tribunal shall give a reasonable opportunity of making representations and of being heard to-

- the Registrar,
- the company and
- all the persons concerned.

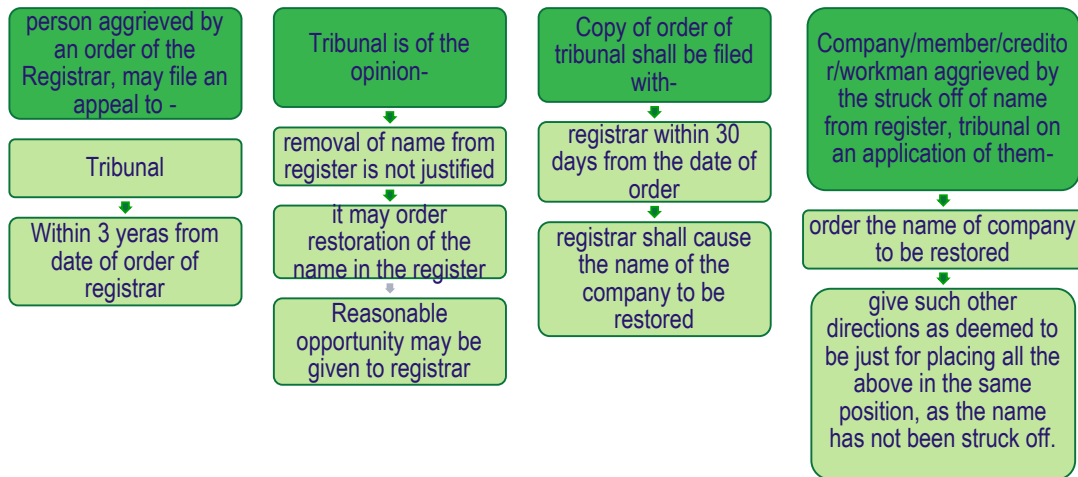
Restoration of name of company: If the Registrar is satisfied, that the name of the company has been struck off from the register of companies either inadvertently or on the basis of incorrect information furnished by the company or its directors, which requires restoration in the register of companies, he may within a period of three years from the date of passing of the order dissolving the company under section 248, file an application before the Tribunal seeking restoration of name of such company.

- (2) **Order of tribunal to be filed with register:** A copy of the order passed by the Tribunal shall be filed by the company with the Registrar within thirty days from the date of the order and on receipt of the order, the Registrar shall cause the name of the company to be restored in the register of companies and shall issue a fresh certificate of incorporation.
- (3) **Order of tribunal as it may deem just:** If a company, or any member or creditor or workman thereof feels aggrieved by the company having its name struck off from the register of companies, the Tribunal on an application made by-
 - the company,
 - member,
 - creditor or
 - workman

before the expiry of twenty years from the publication in the Official Gazette of the notice under sub-section (5) of section 248 may, if satisfied that the company was, at the time of its name being struck off, carrying on business or in operation or otherwise it is just that the name of the company be restored to the register of companies,

- order the name of the company to be restored to the register of companies,
- and the Tribunal may, by the order, give such other directions and make such provisions as deemed just for placing the company and all other persons in the same

position as nearly as may be as if the name of the company had not been struck off from the register of companies.



In a decided case law *Nirendra Nath Kar v. Gopal Navin Bhai Dave*, Civil Appeal No. 4448 of 2015 September 29, 2022, where under Section 252 of the Companies Act, 2013 an appeal to Tribunal was filed on an order of removal of name of company from the Register of companies. Where an application for restoration of company was made by appellant who was neither company nor a member nor a creditor, he could not be said to be a person aggrieved to question order of RoC to strike off name of company from Register of Companies and, thus, appellant had no locus standi to file application for restoration of name of company. Order passed by Division Bench of High Court setting aside order of Single Judge for restoring name of company was held to be justified.



4. GOVERNMENT COMPANIES

[I] Annual reports on Government companies [Section 394]

As per section 2(45) of the Companies Act, 2013, “Government Company” means any company in which not less than 51% of the paid-up share capital (equity & preference) is held by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments, and includes a company which is a subsidiary company of such a Government company.

Explanation: Here “paid up share capital” shall be construed as “total voting power”, where shares with differential voting rights have been issued.

Section 394 of the Companies Act, 2013 provides for Annual reports on Government companies.

It provides for Annual reports on Government companies in the cases where the Central Government and the State Government is a member of the Government Company. According to this section:

- (1) **Where the Central Government is a member of a Government company**, the Central Government shall cause an annual report on the working and affairs of that company to be—
 - (a) prepared within three months of its annual general meeting before which the comments given by the Comptroller and Auditor-General of India and the audit report are placed under the proviso to sub-section (6) of section 143; and
 - (b) as soon as may be after such preparation, laid before both Houses of Parliament together with a copy of the audit report and comments upon or supplement to the audit report, made by the Comptroller and Auditor-General of India.
- (2) **Where in addition to the Central Government, any State Government is also a member of a Government company**, that State Government shall cause a copy of the annual report prepared under sub-section (1) to be laid before the House or both Houses of the State Legislature together with a copy of the audit report and the comments upon or supplement to the audit report referred above.

Example 6:

- (i) Central Government and Government of Maharashtra together hold 40% of the paid-up share capital of MN Limited. A government company also holds 20% of the paid-up share capital in MN Limited.
- (ii) PQ Limited is a subsidiary but not a wholly owned subsidiary of a government company.

Position of MN Limited and PQ Limited as a Government Company.

In this case, MN Limited is not a Government company because the holding of the Central Government and Government of Maharashtra is 40% which is less than the 51% prescribed under the definition of Government Company. The holding of the government company in MN Limited of 20% cannot be taken into account while counting the prescribed limit of 51%.

Whereas in the second case, **PQ Limited is a government company** as the definition of Government Company clearly specifies that a Government Company includes a company which is a subsidiary company of a Government company. Whether the subsidiary should be a wholly owned subsidiary or not is not clearly mentioned under the definition of the Government company under section 2(45).

[II] Annual reports where one or more State Governments are members of companies [Section 395]

Section 395 of the Companies Act, 2013 seeks to provide that where central Government is not a member of Government Company, but one or more state Government(s) are member, then state Government shall prepare annual reports on the working and affairs of the company. According to this section:

- (1) **Where the Central Government is not a member of a Government company**, every State Government which is a member of that company, or where only one State Government is a member of the company, that State Government shall cause an annual report on the working and affairs of the company to be—
 - (a) Prepared within the time specified in sub-section (1) of section 394; and
 - (b) as soon as may be after such preparation, laid before the House or both Houses of the State Legislature together with a copy of the audit report and comments upon or supplement to the audit report referred to in sub-section (1) of that section.
- (2) **Application of the provisions to the Government Company in liquidation:** The provisions of this section and section 394 shall, so far as may be, apply to a Government company in liquidation as it applies to any other Government company.



5. NIDHIS

Power to Modify Act in its Application to Nidhis [Section 406 of the Companies Act, 2013]

Section 406 of the Companies Act, provides power to the Central Government to modify Act in its application to *Nidhis*. According to this section:

- (1) **"Nidhi" or "Mutual Benefit Society"** means a company which the Central Government may, by notification in the Official Gazette, declare to be a Nidhi or Mutual Benefit Society, as the case may be.
- (2) The Central Government may, by notification in the Official Gazette, direct that any of the provisions of this Act specified in the notification—
 - (a) shall not apply to any Nidhi or Mutual Benefit Society; or
 - (b) shall apply to any Nidhi or Mutual Benefit Society with such exceptions, modifications and adaptations as may be specified in the notification.
- (3) A copy of every notification proposed to be issued under sub-section (2), shall be laid in draft before each House of Parliament, while it is in session, for a total period of thirty days, and if, both Houses agree in disapproving the issue of notification or both Houses agree in making any modification in the notification, the notification shall not be issued or, as the case may be, shall be issued only in such modified form as may be agreed upon by both the Houses.
- (4) In reckoning any such period of thirty days as is referred to in sub-section (3), no account shall be taken of any period during which the House referred to in sub-section (3) is prorogued or adjourned for more than four consecutive days.
- (5) The copies of every notification issued under this section shall, as soon as may be after it has been issued, be laid before each House of Parliament.

The Nidhi Rules, 2014 [As amended by Nidhi (Amendment) Rules 2022], shall apply in relation to the following:

Application (Rule 2): These rules shall apply to-

- (a) **every company** which had been declared as a Nidhi or Mutual Benefit Society under sub - section (1) of Section 620A of the Companies Act, 1956,
- (b) **every company functioning on the lines of a Nidhi company or Mutual Benefit Society** but has either not applied for or has applied for and is awaiting notification to be a Nidhi or Mutual Benefit Society under sub- Section (1) of Section 620A of the Companies Act, 1956; and
- (c) **every company incorporated** as a Nidhi pursuant to the provisions of Section 406 of the Act.
- (d) **every company declared as Nidhi or Mutual Benefit Society** under sub-section (1) of section 406 of the Act.

Definitions (Rule 3)

- (a) **"Act"** means the Companies Act, 2013;
- (aa) **"Branch"** means a place other than the registered office of Nidhi"
- (b) **"Doubtful Asset"** means a borrowal account which has remained a non performing asset for more than two years but less than three years;
- (c) **"Loss Asset"** means a borrowal account which has remained a nonperforming asset for more than three years or where in the opinion of the Board, a shortfall in the recovery of the loan account is expected because the documents executed may become invalid if subjected to legal process or for any other reason;
- (d) **"Net Owned Funds"** means the aggregate of paid up equity share capital and free reserves as reduced by accumulated losses and intangible assets appearing in the last audited balance sheet:

Provided that the amount representing the proceeds of issue of preference shares shall not be included for calculating Net Owned Funds.

- (da) **"Nidhi"** means a company which has been incorporated as a nidhi with the object of cultivating the habit of thrift and saving amongst its members, receiving deposits from, and lending to, its members only, for their mutual benefit, and which complies with the rules made by the central Government for regulation of such class of companies.
- (e) **"Non-Performing Asset"** means a borrowal account in respect of which interest income or instalment of loan towards repayment of principal amount has remained unrealised for twelve months;

- (f) **“Standard Asset”** means the asset in respect of which no default in repayment of principal or payment of interest has occurred or is perceived and which has neither shown signs of any problem relating to repayment of principal sum or interest nor does it carry more than normal risk attached to the business;
- (g) **“Sub-Standard Asset”** means a borrowal account which is a non performing asset:
Provided that reschedulement or renegotiation or rephasing of the loan instalment or interest payment shall not change the classification of an asset unless the borrowal account has satisfactorily performed for at least twelve months after such reschedulement or renegotiation or rephasing.

Incorporation and incidental matters (Rule 4)—

- (a) A Nidhi shall be a **public company** and shall have a **minimum paid up equity share capital of 10 lakh rupees**.

Provided that every Nidhi existing as on the date of commencement of the Nidhi Amendment Rules, 2022, shall comply with this requirement within a period of eighteen months from the date of such commencement.

- (b) On and after the commencement of the Act, **no Nidhi shall issue preference shares**.
- (c) If preference shares had been issued by a Nidhi before the commencement of this Act, such preference shares shall be redeemed in accordance with the terms of issue of such shares.
- (d) Except as provided under the proviso to sub-rule (e) to rule 6, no Nidhi shall have any object in its Memorandum of Association other than the **object of cultivating the habit of thrift and savings amongst its members, receiving deposits** from, and lending to, its members only, for their mutual benefit.

Exception as provided under the proviso to sub-rule (e) to rule 6: Nidhis which have adhered to all the provisions of these rules may provide **locker facilities on rent to its members** subject to the rental income from such facilities not exceeding twenty per cent of the gross income of the Nidhi at any point of time during a financial year.

- (e) Every “Nidhi” shall have the last words **‘Nidhi Limited’ as part of its name**.

Requirements for minimum number of members, net owned fund etc. (Rule 5):

- (1) Every Nidhi shall, within a period of one year from the date of its incorporation, ensure that it has—
- (i) not less than two hundred members;
 - (ii) Net Owned Funds of ten lakh rupees or more;
 - (iii) unencumbered term deposits of not less than ten per cent of the outstanding deposits as specified in rule 14; and
 - (iv) ratio of Net Owned Funds to deposits of not more than 1:20.

- (2) Within ninety days from the close of the first financial year after its incorporation and where applicable, the second financial year, Nidhi shall file a return of statutory compliances in Form NDH-1 along with such fee as provided in Companies (Registration Offices and Fees) Rules, 2014 with the Registrar duly certified by a company secretary in practice or a chartered accountant in practice or a cost accountant in practice.
- (3) If a Nidhi is not complying with clauses (i) or (iv) of sub-rule (1) above, it shall within thirty days from the close of the first financial year, apply to the Regional Director in Form NDH-2 along with fee specified in Companies (Registration Offices and Fees) Rules, 2014 for extension of time and the Regional Director may consider the application and pass orders within thirty days of receipt of the application.

Provided that the Regional Director may extend the period upto one year from the date of receipt of application.

Explanation—For the purpose of this rule "Regional Director" means the person appointed by the Central Government in the Ministry of Corporate Affairs as a Regional Director;

- (4) If the failure to comply with sub-rule (1) of this rule extends beyond the second financial year, Nidhi shall not accept any further deposits from the commencement of the second financial year till it complies with the provisions contained in sub-rule (1), and gets itself declared under sub-section (1) of section 406 besides being liable for penal consequences as provided in the Act.
- (5) The provisions of this rule shall not be applicable for the companies incorporated as Nidhi on or after the commencement of the Nidhi (Amendment) Rules, 2022.

General restrictions or prohibitions (Rule 6)—

No Nidhi shall—

- (a) carry on the business of chit fund, hire purchase finance, leasing finance, insurance or acquisition of securities issued by any body corporate;
- (b) issue preference shares, debentures or any other debt instrument by any name or in any form whatsoever;
- (c) open any current account with its members;
- (d) acquire or purchase securities of any other company or control the composition of the Board of Directors of any other company in any manner whatsoever or enter into any arrangement for the change of its management.

Explanation—For the purposes of this sub-rule, "control" shall have the same meaning assigned to it in section 2(27) of the Act;

- (e) carry on any business other than the business of borrowing or lending in its own name:

However, Nidhis which have adhered to all the provisions of these rules may provide locker facilities on rent to its members subject to the rental income from such facilities not exceeding twenty per cent of the gross income of the Nidhi at any point of time during a financial year.

- (f) accept deposits from or lend to any person, other than its members;
- (g) pledge any of the assets lodged by its members as security;
- (h) take deposits from or lend money to any body corporate;
- (i) enter into any partnership arrangement in its borrowing or lending activities;
- (j) issue or cause to be issued any advertisement in any form for soliciting deposit:

However private circulation of the details of fixed deposit Schemes among the members of the Nidhi carrying the words "for private circulation to members only" shall not be considered to be an advertisement for soliciting deposits.

- (k) pay any brokerage or incentive for mobilising deposits from members or for deployment of funds or for granting loans.
- (l) ¹raise loans from banks or financial institutions or any other source for the purpose of advancing loans to members of Nidhi

Example 7: Sunshine Benefit Fund Limited, incorporated as a Nidhi Company under the Companies Act, 2013. The Board of Directors have decided to provide Locker Facilities on rent to its members and have estimated that rental income from such letting would be around 25% of the gross income of the company. In the given case, the Board of Directors cannot provide locker facilities on rent to its member in the light of the requirement of the Rule 6 (e) of the Nidhi Rules, 2014. According to the rule, Nidhis which have adhered to all the provisions of these rules may provide locker facilities on rent to its members subject to the rental income from such facilities not exceeding twenty per cent of the gross income of the Nidhi at any point of time during a financial year.

Share capital and allotment (Rule 7)

- (a) Every Nidhi shall issue fully paid up equity shares of the nominal value of not less than ten rupees each:

Provided that this requirement shall not apply to a company referred to in sub-rules (a) and (b) of rule 2.
- (b) No service charge shall be levied for issue of shares.
- (c) Every Nidhi shall allot to each deposit holder at least a minimum of ten equity shares or shares equivalent to one hundred rupees:

¹ Inserted by the Nidhi (Amendment) Rules, 2022

Provided that a savings account holder and a recurring deposit account holder shall hold at least one equity share of rupees ten.

Membership (Rule 8)—

- (1) A Nidhi shall not admit a body corporate or trust as a member.
- (2) Except as otherwise permitted under the rules, every Nidhi shall ensure that its membership is not reduced to less than 200 members at any time.
- (3) A minor shall not be admitted as a member of Nidhi:
However, deposits may be accepted in the name of a minor, if they are made by the natural or legal guardian who is a member of Nidhi.
- (4) A member shall not transfer more than fifty percent of his shareholding (as on the date of availing of loan or making of deposit) during the subsistence of such loan or deposit, as the case may be.

Provided that the member shall retain the minimum number of shares required under sub-rule (3) of rule 7 at all times.

Net owned funds (Rule 9)

Every Nidhi shall maintain Net Owned Funds (excluding the proceeds of any preference share capital) of not less than twenty lakh rupees or such higher amount as the Central Government may specify from time to time.

Provided that every Nidhi existing as on the date of commencement of the Nidhi (Amendment) Rules, 2022 shall comply with this requirement within a period of eighteen months from the date of such commencement.

Acceptance of Deposits by Nidhis (Rule 11)

- (a) A Nidhi shall not accept deposits exceeding twenty times of its Net Owned Funds (NOF) as per its last audited financial statements.
- (b) In the case of companies covered under clauses (a) and (b) of rule 2 and existing on or before 26th July, 2001 and which have accepted deposits in excess of the aforesaid limits, the same shall be restored to the prescribed limit by increasing the Net Owned Funds position or alternatively by reducing the deposit according to the table given below:

Ratio of Net Owned Funds to Deposits (as on 31.3. 2013)	Date by which the company has to achieve prescribed ceiling of 1:20
(a) More than 1:20 but upto 1:35	By 31.3. 2015
(b) More than 1:35 but upto 1:45	By 31.3. 2016
(c) More than 1:45	By 31.3. 2017

- (c) The companies which are covered under the Table above shall not accept fresh deposits or renew existing deposits if such acceptance or renewal leads to violation of the prescribed ratio.
- (d) The ratio specified in table above shall also apply to incremental deposits.

Deposits (Rule 13)

- (1) The fixed deposits shall be accepted for a minimum period of six months and a maximum period of sixty months.
- (2) Recurring deposits shall be accepted for a minimum period of twelve months and a maximum period of sixty months.
- (3) In case of recurring deposits relating to mortgage loans, the maximum period of recurring deposits shall correspond to the repayment period of such loans granted by *Nidhi*.
- (4) The maximum balance in a savings deposit account at any given time qualifying for interest shall not exceed one lakh rupees at any point of time and the rate of interest shall not exceed two per cent. above the rate of interest payable on savings bank account by nationalised banks.
- (5) A *Nidhi* may offer interest on fixed and recurring deposits at a rate not exceeding the maximum rate of interest prescribed by the Reserve Bank of India which the Non-Banking Financial Companies can pay on their public deposits.
- (6) A fixed deposit account or a recurring deposit account shall be foreclosed by the depositor subject to the following conditions, namely:-
 - (a) a *Nidhi* shall not repay any deposit within a period of three months from the date of its acceptance;
 - (b) where at the request of the depositor, a *Nidhi* repays any deposit after a period of three months, the depositor shall not be entitled to any interest up to six months from the date of deposit;
 - (c) where at the request of the depositor, a *Nidhi* makes repayment of a deposit before the expiry of the period for which such deposit was accepted by *Nidhi*, the rate of interest payable by *Nidhi* on such deposit shall be reduced by two per cent. from the rate which *Nidhi* would have ordinarily paid, had the deposit been accepted for the period for which such deposit had run:

Provided that in the event of death of a depositor, the deposit may be repaid prematurely to the surviving depositor or depositors in the case of joint holding with survivor clause, or to the nominee or to legal heir with interest up to the date of repayment at the rate which the company would have ordinarily paid, had such deposit been accepted for the period for which such deposit had run.

Un-encumbered Term Deposits (Rule 14)

Every Nidhi shall invest and continue to keep invested, in unencumbered term deposits with a scheduled commercial bank (other than a co-operative bank or a regional rural bank), or post office deposits in its own name an amount which shall not be less than ten per cent. of the deposits outstanding at the close of business on the last working day of the second preceding month:

Provided that in cases of unforeseen commitments, temporary withdrawal may be permitted with the prior approval of the Regional Director by making application in Form NDH- 2 alongwith fee specified in the Companies (the Registration Offices and Fees) Rules, 2014 for the purpose of repayment to depositors, subject to such conditions and time limit which may be specified by the Regional Director to ensure restoration of the prescribed limit of ten per cent.

Loans (Rule 15)

- (1) A *Nidhi* shall provide loans only to its members.

Provided that in case of joint shareholders, the loan shall be provided to the member whose name appears first in the Register of members.

- (2) The loans given by a *Nidhi* to a member shall be subject to the following limits, namely:-

- (a) two lakh rupees, where the total amount of deposits of such *Nidhi* from its members is less than two crore rupees;
- (b) seven lakh fifty thousand rupees, where the total amount of deposits of such *Nidhi* from its members is more than two crore rupees but less than twenty crore rupees;
- (c) twelve lakh rupees, where the total amount of deposits of such *Nidhi* from its members is more than twenty crore rupees but less than fifty crore rupees; and
- (d) fifteen lakh rupees, where the total amount of deposits of such *Nidhi* from its members is more than fifty crore rupees:

Provided that where a *Nidhi* has not made profits continuously in the three preceding financial years, it shall not make any fresh loans exceeding fifty per cent. of the maximum amounts of loans specified in clauses (i), (ii), (iii) or (iv).

Provided further that a member shall not be eligible for any further loan if he has borrowed any earlier loan from the *Nidhi* and has defaulted in repayment of such loan.

- (3) For the purposes of sub-rule (2), the amount of deposits shall be calculated on the basis of the last audited annual financial statements.
- (4) A *Nidhi* shall give loans to its members only against the following securities, namely:-
 - (a) gold, silver and jewellery:

Provided that the repayment period of such loan shall not exceed one year.

- (b) immovable property:

Provided that the total loans against immovable property [excluding mortgage loans granted on the security of property by registered mortgage, being a registered mortgage under section 69 of the Transfer of Property Act, 1882] shall not exceed fifty per cent. of the overall loan outstanding on the date of approval by the board, the individual loan shall not exceed fifty per cent. of the value of property offered as security and the period of repayment of such loan shall not exceed seven years.

- (c) fixed deposit receipts, National Savings Certificates, other Government Securities and insurance policies:

Provided that such securities duly discharged shall be pledged with *Nidhi* and the maturity date of such securities shall not fall beyond the loan period or one year whichever is earlier:

Provided further that in the case of loan against fixed deposits, the period of loan shall not exceed the unexpired period of the fixed deposits.

Rate of Interest (Rule 16)

The rate of interest to be charged on any loan given by a *Nidhi* shall not exceed seven and half per cent. above the highest rate of interest offered on deposits by *Nidhi* and shall be calculated on reducing balance method:

Provided that *Nidhi* shall charge the same rate of interest on the borrowers in respect of the same class of loans and the rates of interest of all classes of loans shall be prominently displayed on the notice board at the registered office and each branch office of *Nidhi*.

Rules relating to Directors (Rule 17)—

- (1) The Director shall be a member of *Nidhi*.
- (2) The Director of a *Nidhi* shall hold office for a term up to 10 consecutive years on the Board of *Nidhi*.
- (3) The Director shall be eligible for re-appointment only after the expiration of 2 years of ceasing to be a Director.
- (4) Where the tenure of any Director in any case had already been extended by the Central Government, it shall terminate on expiry of such extended tenure.
- (5) The person to be appointed as a Director shall comply with the requirements of sub-section (4) of Section 152 of the Act and shall not have been disqualified from appointment as provided in section 164 of the Act.

Dividend (Rule 18)—

A *Nidhi* shall not declare dividend exceeding twenty five per cent in a financial year.

Auditor (Rule 19)—

- (1) No Nidhi shall appoint or re-appoint an individual as auditor for more than one term of 5 consecutive years.
- (2) No Nidhi shall appoint or re-appoint an audit firm as auditor for more than 2 terms of 5 consecutive years:

Provided that an auditor (whether an individual or an audit firm) shall be eligible for subsequent appointment after the expiration of 2 years from the completion of his or its term.

Explanation: For the purposes of this proviso:

- (a) in case of an auditor (whether an individual or audit firm), the period for which he or it has been holding office as auditor prior to the commencement of these rules shall be taken into account in calculating the period of 5 consecutive years or 10 consecutive years, as the case may be;
- (b) appointment includes re-appointment.

Filing of Half Yearly Return (Rule 21)

Every company covered Rule 2 shall file half yearly return with the Registrar in Form NDH-3 along with such fees as provided in Companies (Registration Office & fees) Rules, 2014 within thirty days from the conclusion of each half year duly certified by a company secretary in practice or chartered accountant in practice or cost accountant in practice.

Auditor's certificate (Rule 22)

The Auditor of the company shall furnish a certificate every year to the effect that the company has complied with all the provisions contained in the rules and such certificate shall be annexed to the audit report and in case of non-compliance, he shall specifically state the rules which have not been complied with.

Penalty for non-compliance (Rule 24)

If a company to which the Nidhi Rules, 2014 applies contravenes any of the provisions of the prescribed rules, the company and every officer of the company who is in default shall be punishable with fine which may extend to 5,000 rupees, and where the contravention is a continuing one, with a further fine which may extend to 500 rupees for every day after the first during which the contravention continues.

Example 8: Suhani Nidhi Limited proposes to reappoint Mr. Hemant, a director who has completed a term of 10 consecutive years as a director of Nidhi. According to **Rule 17** of the Nidhi Rules 2014, the director of a nidhi company shall hold office for a term upto 10 consecutive years on the board of Nidhi and he shall be eligible for re-appointment only after expiration of two years of ceasing to be a director.

Hence, in the instant case, Suhani Nidhi Limited cannot re-appoint Mr. Hemant as a director for a period of two years after completion of 10 consecutive years.



6. MISCELLANEOUS PROVISIONS

[I] Punishment for fraud [Section 447]

Section 447 of the Companies Act, 2013 provides for Punishment for fraud. According to this section:

- (i) Without prejudice to any liability including repayment of any debt under this Act or any other law for the time being in force, **any person who is found to be guilty of fraud** involving an amount of at least ten lakh rupees or one per cent of the turnover of the company, whichever is lower, shall be punishable with imprisonment for a term which shall not be less than 6 months but which may extend to 10 years and shall also be liable to fine which shall not be less than the amount involved in the fraud, but which may extend to 3 times the amount involved in the fraud.
- (ii) Where the **fraud in question involves public interest**, the term of imprisonment shall not be less than 3 years.
- (iii) Where the **fraud involves an amount less than ₹ 10 Lakhs or one per cent of the turnover** of the company, whichever is lower, and does not involve public interest, any person guilty of such fraud shall be punishable with imprisonment for a term which may extend to five years or with fine which may extend to ²₹ 50 Lakhs or with both.

Explanation—For the purposes of this section—

- (a) “**fraud**” in relation to affairs of a company or any body corporate, includes any act, omission, concealment of any fact or abuse of position committed by any person or any other person with the connivance in any manner, with intent to deceive, to gain undue advantage from, or to injure the interests of, the company or its shareholders or its creditors or any other person, whether or not there is any wrongful gain or wrongful loss;
- (b) “**wrongful gain**” means the gain by unlawful means of property to which the person gaining is not legally entitled;
- (c) “**wrongful loss**” means the loss by unlawful means of property to which the person losing is legally entitled.

[II] Punishment where no specific penalty or punishment is provided [Section 450]

- (i) **Applicability of section 450:** The penalty under this section applies only in those cases where penalty or punishment is not provided elsewhere in this Act.

²Substituted for "twenty lakh rupees" by the Companies (Amendment) Second Ordinance, 2019, w.r.e.f. 2-11-2018.

- (ii) **Penalty under this section:** The company and every officer of the company who is in default or such other person:
- shall be liable to a penalty of ₹ 10,000, and
 - Where the contravention is continuing one, with a further penalty of one thousand rupees for each day after the first during which the contravention continues, subject to a maximum of two lakh rupees in case of a company and fifty thousand rupees in case of an officer who is in default or any other person
- (iii) **List of contraventions:** If a company or any officer of a company or any other person contravenes:
- any of the provisions of this Act; or
 - the rules made thereunder; or
 - any condition, limitation or restriction subject to which any approval, sanction, consent, confirmation, recognition, direction or exemption in relation to any matter has been accorded, given or granted.

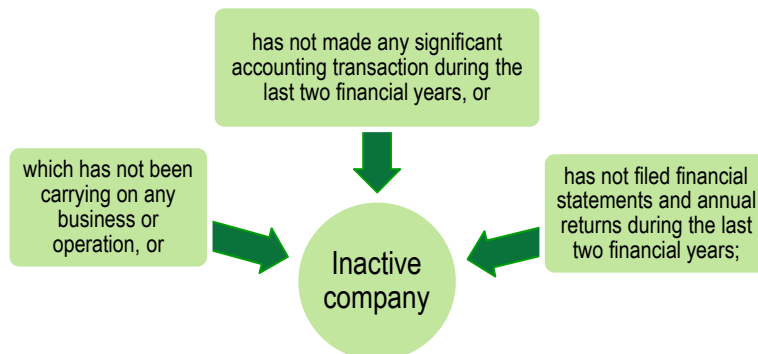
[III] Dormant company [Section 455]

Section 455 of the Companies Act, 2013 provides for Dormant Company. According to this section:

- (i) **Status as a dormant company:** Where a company is formed and registered under this Act for a future project or to hold an asset or intellectual property and has no significant accounting transaction, such a company or an inactive company may make an application to the Registrar in such manner as may be prescribed for obtaining the status of a dormant company.

Explanation—For the purposes of this section,—

- (a) **“inactive company”** means a company which has not been carrying on any business or operation, or has not made any significant accounting transaction during the last two financial years, or has not filed financial statements and annual returns during the last two financial years;



- (b) “**significant accounting transaction**” means any transaction other than—
- (1) payment of fees by a company to the Registrar;
 - (2) payments made by it to fulfill the requirements of this Act or any other law;
 - (3) allotment of shares to fulfill the requirements of this Act; and
 - (4) payments for maintenance of its office and records.

According to the Rule 3 of the Companies (Miscellaneous) Rules, 2014, a company may make an application in Form *MSC-1* along with such fee as provided in the Companies (Registration Offices and Fees) Rules, 2014 to the Registrar for obtaining the status of a Dormant Company in accordance with the provisions of section 455 after passing a special resolution to this effect in the general meeting of the company or after issuing a notice to all the shareholders of the company for this purpose and obtaining consent of at least 3/4th shareholders (in value).

A company shall be eligible to apply under this rule only, if-

- (a) no inspection, inquiry or investigation has been ordered or taken up or carried out against the company;
 - (b) no prosecution has been initiated and pending against the company under any law;
 - (c) the company is neither having any public deposits which are outstanding nor the company is in default in payment thereof or interest thereon;
 - (d) the company is not having any outstanding loan, whether secured or unsecured:
However if there is any outstanding unsecured loan, the company may apply under this rule after obtaining concurrence of the lender and enclosing the same with Form *MSC-1*;
 - (e) there is no dispute in the management or ownership of the company and a certificate in this regard is enclosed with Form *MSC-1*;
 - (f) the company does not have any outstanding statutory taxes, dues, duties etc. payable to the Central Government or any State Government or local authorities etc.;
 - (g) the company has not defaulted in the payment of workmen's dues;
 - (h) the securities of the company are not listed on any stock exchange within or outside India.
- (ii) **Certificate of status of dormant company:** The Registrar on consideration of the application shall allow the status of a dormant company to the applicant and issue a certificate in such form as may be prescribed to that effect.

According to the Rule 4 of the Companies (Miscellaneous) Rules, 2014, the Registrar shall, after considering the application filed in Form *MSC-1*, issue a certificate in Form *MSC-2* allowing the status of a Dormant Company to the applicant.

- (iii) **Register of dormant company:** The Registrar shall maintain a register of dormant companies in such form as may be prescribed.

According to the Rule 5 of the Companies (Miscellaneous) Rules, 2014, the Register maintained under the portal maintained by the Ministry of Corporate Affairs on its web-site www.mca.gov.in or any other website notified by the Central Government, shall be the register for dormant companies.

- (iv) **Consequences of non-filing of annual returns or financial statements:** In case of a company which has not filed financial statements or annual returns for 2 financial years consecutively, the Registrar shall issue a notice to that company and enter the name of such company in the register maintained for dormant companies.

According to the Rule 7 of the Companies (Miscellaneous) Rules, 2014, a dormant company shall file a "Return of Dormant Company" annually, *inter alia*, indicating financial position duly audited by a chartered accountant in practice in Form MSC-3 along with such annual fee as provided in the Companies (Registration Offices and Fees) Rules, 2014 within a period of 30 days from the end of each financial year.

The company shall also continue to file the return or returns of allotment and change in directors in the manner and within the time specified in the Act, whenever the company allots any security to any person or there is any change in the directors of the company.

Example 9: ABC Company was incorporated in the year 2010. The Company did not file its financial statement with Registrar of Companies for the year 2018-19. Due to financial losses the Company is neither carrying on any business nor did any significant account transactions from the past one and half year. In July 2020 the company decided to file the application for obtaining the status of inactive company.

As per section 455(1), such an inactive company (company which has not been carrying on any business or operation, or has not made any significant accounting transaction during the last two financial years, or has not filed financial statements and annual returns during the last two financial years) may make an application to the Registrar for obtaining the status of a dormant company.

- (v) **Directors of dormant company:** A dormant company shall have such minimum number of directors, file such documents and pay such annual fee as may be prescribed to the Registrar to retain its dormant status in the register and may become an active company on an application made in this behalf accompanied by such documents and fee as may be prescribed.

According to Rule 6 of the Companies (Miscellaneous) Rules, 2014, a dormant company shall have a minimum number of 3 directors in case of a public company, 2 directors in case of a private company and 1 director in case of a One Person Company.

Rotation of auditors: According to Rule 6 the Companies (Miscellaneous) Rules, 2014, the provisions of the Act in relation to the rotation of auditors shall not be applicable to dormant companies.

Application for seeking status of an active company: According to the Rule 8 of the Companies (Miscellaneous) Rules, 2014,

- (a) **Filing of an application:** An application for obtaining the status of an active company shall be made in Form *MSC-4* along with fees as provided in the Companies (Registration Offices and Fees) Rules, 2014 and shall be accompanied by a return in Form *MSC-3* in respect of the financial year in which the application for obtaining the status of an active company is being filed:

However, the Registrar shall initiate the process of striking off the name of the company if the company remains as a dormant company for a period of consecutive 5 years.
- (b) **Issue of certificate by Registrar:** The Registrar shall, after considering the application filed for obtaining the status of an active company, issue a certificate in Form *MSC-5* allowing the status of an active company to the applicant.
- (c) **Filing of an application by Directors on doing or omission of act by dormant company:** Where a dormant company does or omits to do any act mentioned in the Grounds of application in Form *MSC-1* submitted to Registrar for obtaining the status of dormant company, affecting its status of dormant company, the directors shall within 7 days from such event, file an application for obtaining the status of an active company.
- (d) **Initiation of proceedings for enquiry:** Where the Registrar has reasonable cause to believe that any company registered as 'dormant company' under his jurisdiction has been functioning in any manner, directly or indirectly, he may initiate the proceedings for enquiry under section 206 of the Act and if, after giving a reasonable opportunity of being heard to the company in this regard, it is found that the company has actually been functioning, the Registrar may remove the name of such company from register of dormant companies and treat it as an active company.
- (vi) **Striking off the name by the Registrar:** The Registrar shall strike off the name of a dormant company from the register of dormant companies, which has failed to comply with the requirements of this section.

TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. With an Authorised Capital of ₹ 45,00,000 (divided into 4,50,000 equity shares of ₹ 10 each) and issued and paid-up capital of ₹ 25,00,000 (divided into 2,50,000 equity shares of ₹ 10 each), Amber Prabhat Nidhi Limited incorporated in 2018 at Balaghat, Madhya Pradesh by Loknath, Premnath and other trusted people, wants to issue a certain number of preference shares to its members. Being the Financial Advisor of Amber Prabhat Nidhi Limited, you are required to advise regarding the quantum of Preference shares which can issued to the members by choosing the correct option from those given below:
 - (a) Amber Prabhat Nidhi Limited can issue Preference Shares equivalent to Authorised Equity Share Capital after carrying out due amendment in the Capital Clause.
 - (b) Amber Prabhat Nidhi Limited cannot issue Preference Shares.
 - (c) Amber Prabhat Nidhi Limited can issue Preference Shares upto 50% of the Authorised Equity Share Capital after carrying out due amendment in the Capital Clause
 - (d) Amber Prabhat Nidhi Limited can issue Preference Shares upto 75% of the Authorised Equity Share Capital after carrying out due amendment in the Capital Clause
2. Who amongst the following may file an application for the restoration of the name of the company in the register of company and within the period of:
 - (a) The Company itself and within 2 years from the date of passing of the order dissolving the company
 - (b) The authorised officials of the company and within 2 years from the date of passing of the order dissolving the company
 - (c) NCLT and within 3 years from the date of passing of the order dissolving the company
 - (d) Any person aggrieved by an order of the Registrar and within 3 years from the date of passing of the order dissolving the company
3. Within how many days authority will grant certificate of registration to the applicant to carry on the activities of a registered valuer?
 - (a) within 30 days of the receipt of application, including the time given by the authority for presenting additional documents, information or clarification, or appearing in person, as the case may be.
 - (b) within 45 days of receipt of the application, including the time given by the authority for presenting additional documents, information or clarification, or appearing in person, as the case may be.

- (c) *within 60 days of receipt of the application, excluding the time given by the authority for presenting additional documents, information or clarification, or appearing in person, as the case may be.*
 - (d) *within 90 days of receipt of the application, excluding the time given by the authority for presenting additional documents, information or clarification, or appearing in person, as the case may be*
4. *A workman aggrieved by the company having its name struck off from the register of companies, applies to Tribunal for after 15 years of the publication of strikeoff of the name of the company in the gazette. Comment on the validity of filing of application by workman in the light of the companies Act, 2013:*
- (a) *Workman is not eligible to file an application for restoration of name of the company in the register of companies.*
 - (b) *Only Company is eligible to file an application for restoration of name of the company in the register of companies but before expiry of 20 years of the notice from the publication in the Official Gazette.*
 - (c) *Workman is eligible to file an application for restoration of name of the company in the register of companies but before expiry of 20 years of the notice from the publication in the Official Gazette.*
 - (d) *Company, member, creditor or a workman are eligible to file an application for restoration of name of the company in the register of companies but after expiry of 20 years of the notice from the publication in the Official Gazette.*
5. *Pankaj Nidhi Limited, incorporated under section 406 of the Companies Act, 2013. Pankaj Nidhi Limited wants to enter into an agreement for acquiring another company by purchase of its securities. Now the management of the Pankaj Nidhi Limited is in dilemma with respect to the requirement of entering into such an agreement. Pankaj Nidhi Limited approached you to provide with the best course of action considering the provisions of the Companies Act, 2013.*
- (a) *As per the Nidhi Rules, 2014, Nidhi company can enter into an agreement for acquiring other company by purchase of its securities provided the Nidhi company has passed a special resolution in its general meeting and also obtained the previous approval of the Regional Director having jurisdiction over such Nidhi.*
 - (b) *As per the Nidhi Rules, 2014, Nidhi Company can acquire or purchase securities of any other company or control the composition of the Board of Directors of any other company in any manner whatsoever or enter into any arrangement for the change of its management.*
 - (c) *As per the Nidhi Rules, 2014, Nidhi company can enter into an agreement for acquiring other company by purchase of its securities provided the Nidhi company has passed a*

special resolution in its general meeting and have obtained the previous approval of the Registrar of Companies (Roc) having jurisdiction over such Nidhi.

- (d) As per the Nidhi Rules, 2014, Nidhi company can enter into an agreement for acquiring other company by purchase of its securities provided the Nidhi company has passed a special resolution in its general meeting or have obtained the previous approval of the Registrar of Companies (Roc) having jurisdiction over such Nidhi.

Descriptive Questions

1. Explain the meaning of 'Fraud' in relation to the affairs of a company and the punishment provided for the same in Section 447 of the Companies Act, 2013.
2. JKL Research Development Limited is a registered Public Limited Company. The company has a unique business idea emerging from research and development in a new area. However, it is a future project and the company has no significant accounting transactions and business activities at present. The company desires to obtain the status of a 'Dormant Company'. Advise the company regarding the provisions of the Companies Act, 2013 in this regard and the procedure to be followed in this regard.
3. Gulmohar Ltd. is a company registered in India for last 5 years. Since last 2 financial years, it has not been carrying on any business or operations and has not filed financial statements and annual returns saying that it has not made any significant accounting transaction during the last two financial years. Considering the current situation, Directors of the Company is contemplating to apply to Registrar of Companies to obtain status of dormant or inactive company. Advise them on:

Whether Gulmohar Ltd. is eligible to apply to Registrar of Companies to obtain dormant status for the company?

- (i) Will your answer be different if Gulmohar Ltd is continuing payment of fees to Registrar of Companies and payment of rentals for its office and accounting records for last two financials years?
- (ii) Is special resolution in general meeting a pre-requisite to make an application to Registrar of Companies for obtaining the status of dormant company?
- (iii) What will be your answer if it is found after making an application of dormant company to Registrar of Companies that an investigation is pending against the company which was ordered 6 months ago?

ANSWERS

Answer to Multiple Choice Questions

1.	b	2.	d	3.	c	4.	c	5.	b

Answer to Descriptive Questions

1. As per the explanation given to section 447 of the Companies Act, 2013, 'Fraud' in relation to affairs of a company or anybody corporate, includes any act, omission, concealment of any fact or abuse of position committed by any person or any other person with the connivance in any manner, with intent to deceive, to gain undue advantage from, or injure the interests of, the company or its shareholders or its creditors or any other person, whether or not there is any wrongful gain or wrongful loss.

"Wrongful gain" means the gain by unlawful means of property to which the person gaining is not legally entitled.

"Wrongful loss" means, the loss by unlawful means of property to which the person losing is legally entitled.

Punishment:

- (i) Without prejudice to any liability including repayment of any debt under this Act or any other law for the time being in force, any person who is found to be guilty of fraud involving an amount of at least ten lakh rupees or one per cent of the turnover of the company, whichever is lower, shall be punishable with imprisonment for a term which shall not be less than six months but which may extend to ten years and shall also be liable to fine which shall not be less than the amount involved in the fraud, but which may extend to three times the amount involved in the fraud.
 - (ii) Where the fraud in question involves public interest, the term of imprisonment shall not be less than three years.
 - (iii) However, where the fraud involves an amount less than ten lakh rupees or one per cent of the turnover of the company, whichever is lower, and does not involve public interest, any person guilty of such fraud shall be punishable with imprisonment for a term which may extend to five years or with fine which may extend to fifty lakh rupees or with both.
2. The provisions related to the Dormant companies is covered under section 455 of the Companies Act, 2013. According to provisions-
- 1. a company is formed and registered under this Act for the purpose of a future project or to hold an asset or intellectual property and has no significant accounting transaction.
 - 2. Such company or an inactive company may make an application to the Registrar in such manner as may be prescribed for obtaining the status of a dormant company.
 - 3. The Registrar shall allow the status of a dormant company to the applicant and issue a certificate after consideration of the application.

4. The Registrar shall maintain a register of dormant companies in such form as may be prescribed.

In case of a company which has not filed financial statements or annual returns for two financial years consecutively, the Register shall issue a notice to that company and enter the name of such company in the register maintained for dormant companies.

A dormant company shall have such minimum number of directors, file such documents and pay such annual fee as may be prescribed to the Registrar to retain its dormant status in the register and may become an active company on an application made in this behalf accompanied by such documents and fee as may be prescribed. However, the Registrar shall strike off the name of a dormant company from the register of dormant companies, which has failed to comply with the requirements of this section.

Thus, JKL Research Development Limited may follow the above procedure to obtain the status of a 'Dormant Company'.

3. (i) According to section 455 of the Companies Act, 2013, an inactive company may make an application to the Registrar in such manner as may be prescribed for obtaining the status of a dormant company.

Here, "*inactive company*" means a company which has not been carrying on any business or operation, or has not made any significant accounting transaction during the last two financial years, or has not filed financial statements and annual returns during the last two financial years.

Gulmohar Ltd., since from last two years is not carrying on business or operations and has not filed financial statements and annual returns saying it has not made any significant accounting transaction during the last two financial years. Thus, it falls within the definition of inactive company as stated above and hence is eligible to apply to Registrar of Companies to obtain the status of Dormant Company.

- (ii) According to Explanation to section 455, "*significant accounting transaction*" means any transaction other than—

- (1) payment of fees by a company to the Registrar;
- (2) payments made by it to fulfill the requirements of this Act or any other law;
- (3) allotment of shares to fulfill the requirements of this Act; and
- (4) payments for maintenance of its office and records.

Thus, Gulmohar Ltd. is still eligible to apply to the Registrar of Companies to obtain the status of Dormant company even if it has continued 'payment of fees to Registrar of Companies and payment of rentals for its office and accounting records' for last

two years, as these transactions have been kept outside the purview of significant accounting transactions.

- (iii) According to the Rule 3 of the *Companies (Miscellaneous) Rules, 2014*, a company may make an application in prescribed form to the Registrar for obtaining the status of a Dormant Company in accordance with the provisions of section 455 after passing a special resolution to this effect in the general meeting of the company or after issuing a notice to all the shareholders of the company for this purpose and obtaining consent of at least 3/4th shareholders (in value).

Thus, special resolution is a pre- requisite to make an application to Registrar of Companies for obtaining the status of dormant company.

- (iv) According to the Rule 3 of the *Companies (Miscellaneous) Rules, 2014*, a company shall be eligible to apply under this rule only, if no inspection, inquiry or investigation has been ordered or taken up or carried out against the company.

According to section 455(6), the Registrar shall strike off the name of a dormant company from the register of dormant companies, which has failed to comply with the requirements of section 455.

In the given case, Gulmohar Ltd. was not eligible to apply for the status of a dormant company as an investigation was pending against the company which was ordered 6 months ago. But since, it has already made an application and then it came to the light about the pending investigation against the company, the Registrar shall not register it as a dormant company and if already registered as a dormant company, strike off the name of a dormant company from the register of dormant companies as the company has contravened the necessary requirements.

[illegible]

CHAPTER

9

ADJUDICATION, SPECIAL COURTS, NATIONAL COMPANY LAW TRIBUNAL & NATIONAL COMPANY LAW APPELLATE TRIBUNAL



LEARNING OUTCOMES

At the end of this Chapter, students will be able to –

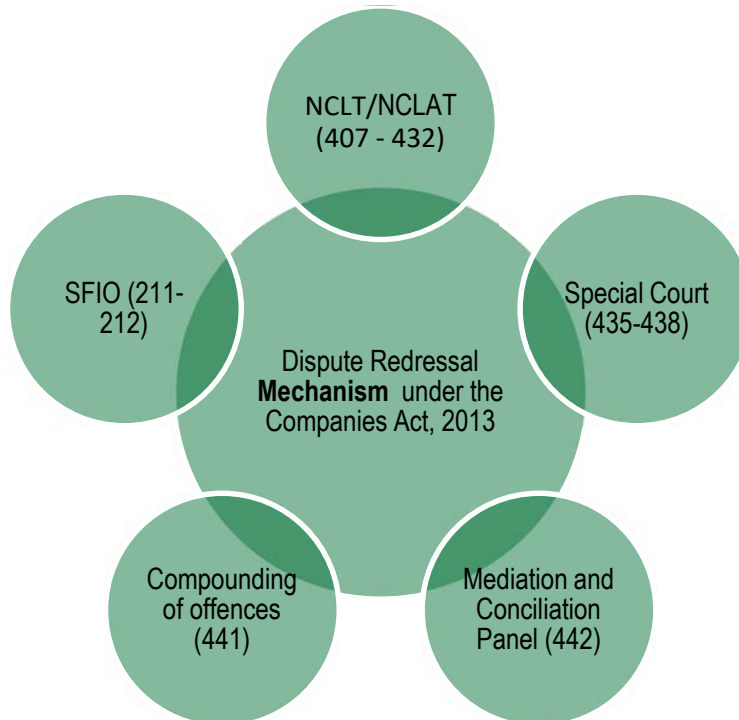
- ❑ Know about the various dispute resolution mechanism
- ❑ Explain the importance and need of NCLT and NCLAT, its working and appeal process and provisions related to transfer of pending proceedings.
- ❑ Identify the establishment of special courts and its Jurisdiction.
- ❑ Know of the procedure of appeal and revision.
- ❑ Elaborate about the Mediation and Conciliation Panel and its working.
- ❑ Determine the process of compounding of offences.
- ❑ Know of the power of Central Government to appoint company prosecutors, provisions related to appeal against acquittal, compensation for accusation and application that can be applied for imposing of fine.
- ❑ Explain the procedure related to adjudication of penalties.



1. INTRODUCTION

A dispute resolution mechanism is a process that deals with disputes arising between two or more parties involved in business or legal relationships.

Under the Companies Act 2013, following are dispute resolution mechanisms or forums:



Establishment of various Adjudication forums under the Companies Act 2013 with regard to the compounding of offences, Special court, and the establishment of mediation panel, SFIO, NCLT and NCLAT is a boon to ensure speedy and efficient resolution of company related disputes in India.

The setting up National Company Law Tribunal (NCLT) and National Company Law Appellate Tribunal (NCLAT) with an objective of establishing a single forum to adjudicate all disputes relating to companies in India. This setting up a single forum dealing with all the matters under the Companies Act 1956 was not new and was introduced earlier by the Companies (Second Amendment) Act, 2002.

However, it was never notified due to challenge of the constitutional validity of the NCLT and NCLAT by Madras High court. However, the Supreme Court gave a ruling that the provisions of Companies (Second Amendment) Act, 2002 pertaining to transfer of several judicial and quasi-judicial powers under the Act to NCLT are constitutionally valid while holding that the qualifications of technical members and the Composition of selection committee of such members as prescribed in the statute had defects and that required correction.



2. NCLT AND NCLAT [SECTION 407 – 434]

The Companies Act, 2013 provides for the constitution of National Company Law Tribunal (NCLT) & National Company Law Appellate Tribunal (NCLAT). NCLT is set up to bring all lawsuits pertaining to companies under one body. It has replaced the Company Law Board (CLB), the Board for Industrial and Financial Reconstruction (BIFR) and the Appellate Authority for Industrial and Financial Reconstruction and will have judicial and technical members.

Vide Ministry of Corporate Affairs Notification S.O.1936 (E) dated 1st June 2016 read with section 434(1) (a) of the Companies Act, 2013, the Central Government hereby appoints the 1st day of June, 2016, on which all matters or proceedings or cases pending before the Board of Company Law Administration (Company Law Board) shall stand transferred to the National Company Law Tribunal and it shall dispose of such matters or proceedings or cases in accordance with the provisions of the Companies Act, 2013 or the Companies Act, 1956.

The provisions dealing with the various parts of NCLT and NCLAT are covered under the Chapter XXVII of the Companies Act, 2013.

NCLT is a quasi-judicial body that adjudicates matters pertaining to companies in India. The National Company Law Tribunal consisting of a President and such number of (Judicial and Technical) members, as the Central Government may deem necessary, to be appointed by notification, to exercise and discharge such powers and functions as conferred on it by or under this Act or any other law for the time being in force. [Section 408]

Any person aggrieved by the decision of NCLT may prefer an appeal to **NCLAT**. The Central Government shall, by notification constitute with effect from such date as may be specified therein, an Appellate Tribunal to be known as the National Company Law Appellate Tribunal consisting of a Chairperson and such number of judicial and technical members, as the Central Government may deem fit, for hearing appeals against, -

- (a) The order of the Tribunal or of the National Financial Reporting Authority under this Act; and
- (b) Any direction, decision or order referred to in section 53A of the Competition Act, 2002 in accordance with the provisions of that Act. [Section 410]

NCLT and NCLAT has provided a single window for settlement of all disputes relating to companies. Further, the provisions of the Insolvency and Bankruptcy Code, 2016 have already been incorporated in the Companies Act, thereby providing a complete harmony in working of NCLT in line with the Insolvency and Bankruptcy Code, 2016. Thus, NCLT and NCLAT is providing a one stop solution to almost all the disputes of the companies under the Companies Act, 2013.

Definitions [Section 407]

Section 407 of the Companies Act, 2013 explains chairperson, judicial members, member, president and technical member who all may be constituting the NCLT & NCLAT. The section defines the following key members –

		Definitions
Chairperson	Means	the Chairperson of the Appellate Tribunal
Judicial Member		a member of the Tribunal or the Appellate Tribunal appointed as such and includes the President or the Chairperson, as the case may be.
Member		a member, whether Judicial or Technical of the Tribunal or the Appellate Tribunal and includes the President or the Chairperson, as the case may be.
President		the President of the Tribunal
Technical Member		a member of the Tribunal or the Appellate Tribunal appointed as such

Order of Tribunal [Section 420]

- (1) **Reasonable opportunity of being heard:** The Tribunal may, after giving the parties to any proceeding before it, a reasonable opportunity of being heard, pass such orders thereon as it thinks fit.
- (2) **Amendment in order:** The Tribunal may, **at any time within 2 years from the date of the order**, with a view **to rectifying any mistake apparent from the record**, amend any order passed by it, and shall make such amendment, if the mistake is brought to its notice by the parties:
Provided that no such amendment shall be made in respect of any order against which an appeal has been preferred under this Act.
- (3) **Send the copy of order to parties concerned:** The Tribunal shall send a copy of every order passed under this section to all the parties concerned.

Example 1: An order made by NCLT was challenged in NCLAT by ABC Ltd. within 1 month of passing of such an order by NCLT. In the meantime, during the pendency of an appeal, one of the party to the NCLT suit notices mistake in the order passed by the NCLT. Accordingly the party files an application against the mistake for its rectification before NCLT. As per section 420 of the Companies Act, the Tribunal may, at any time within 2 years from the date of the order, with a view to rectifying any mistake apparent from the record, amend any order passed by it, and shall make such amendment, if the mistake is brought to its notice by the parties. But no such amendment shall be made in respect of any order against which an appeal has been preferred under this Act. Therefore, application made by the party for rectification of error in the order, cannot be made.

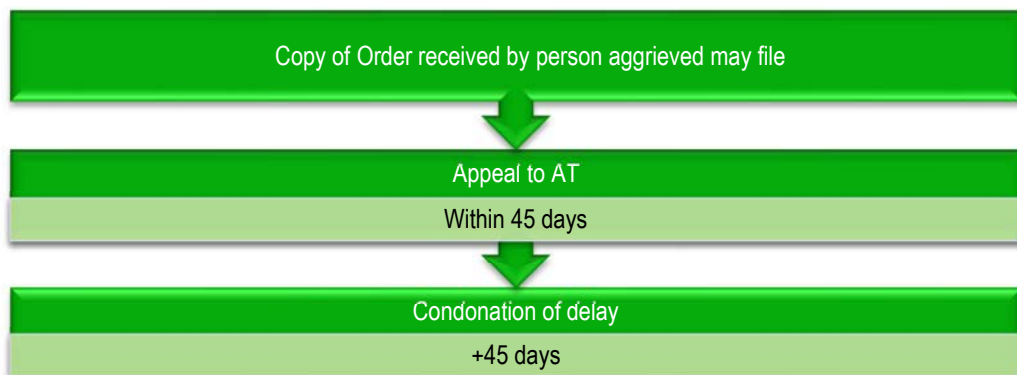
Anubhav Anilkumar Agarwal v. Bank of India, Company Appeal (AT) (Insolvency) No. 1504 of 2019, December 7, 2020, In this case it was held that Power of review has not been expressly conferred upon NCLAT under rule 11 of NCLAT Rules. However, said power under rule 11 can only be exercised for correction of a mistake.

Appeal from Orders of Tribunal [Section 421]

- (1) **Appeal to AT:** Any person aggrieved by an order of the Tribunal may prefer an appeal to the Appellate Tribunal (AT).
- (2) **When order made by consent of parties:** No appeal shall lie to the Appellate Tribunal from an order made by the Tribunal with the consent of parties.
- (3) **Period for filing of appeal:** Every appeal under sub-section (1) (i.e., appeal to AT against order of Tribunal) shall be filed within a period of 45 days from the date on which a copy of the order of the Tribunal is made available to the person aggrieved and shall be in such form, and accompanied by such fees, as may be prescribed:

Provided that the Appellate Tribunal may entertain an appeal after the expiry of the said period of 45 days from the date aforesaid, but within a further period not exceeding 45 days, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within that period.

Explanation: It is to be understood that it is solely at the discretion of the Tribunal whether to provide extension or not by such number of days which shall however not exceed 45 days.



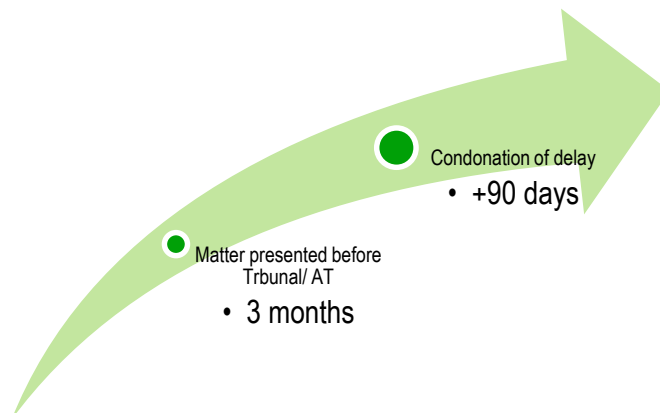
- (4) **Pass order after giving of reasonable opportunity of being heard:** On the receipt of an appeal under sub-section (1), the Appellate Tribunal shall, after giving the parties to the appeal a reasonable opportunity of being heard, pass such orders thereon as it thinks fit, confirming, modifying or setting aside the order appealed against.
- (5) **Copy of order to tribunal and parties to appeal:** The Appellate Tribunal shall send a copy of every order made by it to the Tribunal and the parties to appeal.

Zee Entertainment Enterprises Ltd. v. Invesco Developing Markets Fund, Company Appeal (AT) No. 121 of 2021, October 7, 2021, it was decided that where respondent, a shareholder of Appellant Company had filed petition before NCLT for holding of Extraordinary General Meeting of appellant as soon as possible and NCLT by impugned order granted only two days to appellant to file its reply to said petition, NCLT had committed an error in not granting reasonable and sufficient time for filing a reply. Therefore, reasonable and sufficient opportunity should be given to appellant for filing a reply and after hearing both parties, NCLT should proceed further.

Expeditious Disposal by Tribunal and Appellate Tribunal [Section 422]

- (1) **Speedy disposal:** Every application or petition presented before the Tribunal and every appeal filed before the Appellate Tribunal shall be dealt with and disposed of by it as expeditiously as possible and every endeavor shall be made by the Tribunal or the Appellate Tribunal, as the case may be, for the disposal of such application or petition or appeal **within 3 months from the date of its presentation** before the Tribunal or the filing of the appeal before the Appellate Tribunal.
- (2) **Reasons to be recorded for delay:** Where any application or petition or appeal is not disposed of within the period specified in sub-section (1), the Tribunal or, as the case may be, the Appellate Tribunal, shall record the reasons for not disposing of the application or petition or the appeal, as the case may be, within the period so specified; and the President or the Chairperson, as the case may be, may, after taking into account the reasons so recorded, extend the period referred to in sub-section (1) by such period not exceeding ninety days as he may consider necessary.

Explanation: The President or the Chairperson, as the case may be, are at a liberty to provide extension with any number of days which shall however not exceed ninety days. Further such extension is not mandatory in nature. If the President or the Chairperson, as the case may be, are of the view that no extension is to be provided, then they may not extend the period for disposing of the application or petition or appeal, as the case may be.



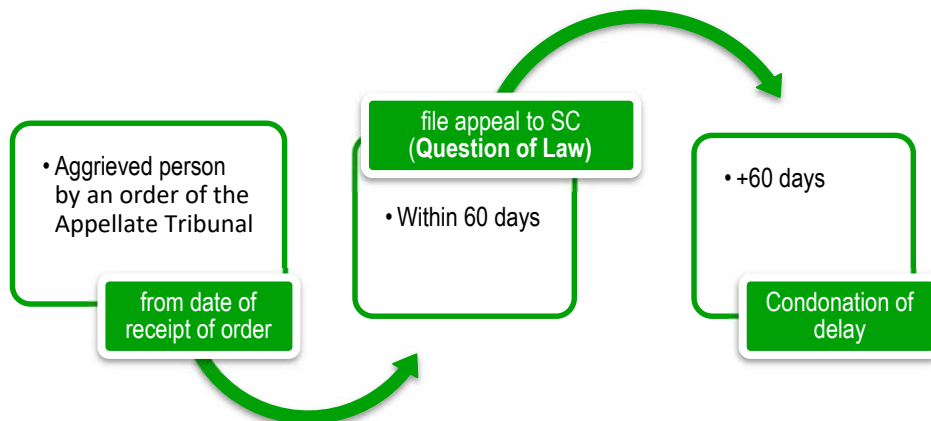
Example 2: Business of ABC Ltd. a public company is not been conducted and managed by directors in accordance with sound business principles or prudent commercial practices. The shareholders of Company has referred the same to the Tribunal on 15th September 2019 with a request to the Tribunal to inquire into the case and take action against the director of company. The Tribunal has, after making proper inquiry, passed the order against the directors on 16th March, 2020. In the given case order passed is not valid, as Tribunal have to pass order within 3 month from date of application and if not possible in 3 month then extension may be possible (if valid reason) for further 90 days i.e., latest by 14th March, 2020.

Appeal to Supreme Court [Section 423]

Any person aggrieved by any order of the Appellate Tribunal may file an appeal to the Supreme Court within 60 days from the date of receipt of the order of the Appellate Tribunal to him on any question of law arising out of such order:

Provided that the Supreme Court may, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within the said period, allow it to be filed within a further period not exceeding 60 days.

Explanation: It is to be understand that it is solely at the discretion of the Supreme Court whether to provide extension or not by such number of days which shall however not exceed 60 days.



Procedure before Tribunal and Appellate Tribunal [Section 424]

- (1) **Tribunal regulate their own procedure based on natural justice:** The Tribunal and the Appellate Tribunal shall not, while disposing of any proceeding before it or, as the case may be, an appeal before it, be bound by the procedure laid down in the Code of Civil Procedure, 1908, but shall be guided by the principles of natural justice, and, subject to the other provisions of this Act or the Insolvency and Bankruptcy Code, 2016 and of any rules made there under, the Tribunal and the Appellate Tribunal shall have power to regulate their own procedure.

- (2) **Vested with same power as that of a civil court:** The Tribunal and the Appellate Tribunal shall have, for the purposes of discharging their functions under this Act or under the Insolvency and Bankruptcy Code, 2016, the same powers as are vested in a civil court under the Code of Civil Procedure, 1908 while trying a suit in respect of the following matters, namely: —
- (a) **summoning** and enforcing the attendance of any person and examining him on oath.
 - (b) requiring the discovery and **production** of documents.
 - (c) receiving **evidence** on affidavits.
 - (d) subject to the provisions of sections 123 and 124 of the Indian Evidence Act, 1872, requisitioning any **public record or document** or a copy of such record or document from any office;
 - (e) issuing commissions for the **examination** of witnesses or documents.
 - (f) **dismissing a representation** for default or deciding it *ex parte*.
 - (g) **setting aside** any order of dismissal of any representation for default or any order passed by it *ex parte*; and
 - (h) **any other matter** which may be prescribed.
- (3) **Nature of decree and its execution:** Any order made by the Tribunal or the Appellate Tribunal may be enforced by that Tribunal in the same manner as if it were a decree made by a court in a suit pending therein, and it shall be lawful for the Tribunal or the Appellate Tribunal to send for execution of its orders to the court within the local limits of whose jurisdiction,—
- (a) in the case of an order against a company, the registered office of the company is situate; or
 - (b) in the case of an order against any other person, the person concerned voluntarily resides or carries on business or personally works for gain.
- (4) **Nature of proceedings:** All proceedings before the Tribunal or the Appellate Tribunal shall be deemed to be judicial proceedings within the meaning of sections 193 and 228, and for the purposes of section 196 of the Indian Penal Code, and the Tribunal and the Appellate Tribunal shall be deemed to be civil court for the purposes of section 195 and Chapter XXVI of the Code of Criminal Procedure, 1973.

Power to punish for contempt [Section 425]

The Tribunal and the Appellate Tribunal shall have the same jurisdiction, powers and authority in respect of contempt of themselves as the High Court has and may exercise, for this purpose, the powers under the provisions of the Contempt of Courts Act, 1971, which shall have the effect subject to modifications that—

- (a) the **reference therein to a High Court** shall be construed as including a reference to the Tribunal and the Appellate Tribunal; and
- (b) the **reference to Advocate-General** in section 15 of the said Act shall be construed as a reference to such Law Officers as the Central Government may, specify in this behalf.

HSBC Daisy Investments (Mauritius) Ltd. V. Anil Dhirubhai Ambani, Contempt Case (AT) Nos. 14 of 2018 & 3 of 2019 Company Appeal (AT) No.99 of 2018, July 23, 2019, it was decided that where consent terms had been arrived between petitioner and contemnors i.e. Reliance Inratel Ltd., by Appellate Tribunal's order dated 29-6-2018 and petitioners preferred contempt petitions under section 425 for initiating proceedings for contempt of disobedience of Appellate Tribunal's order dated 29-6-2018 alleging willful breach of undertaking given by contemnors, not following of 'Consent Terms' cannot be a ground for initiation of a contempt proceeding, and, therefore, no case was made out for initiation of contempt proceedings against any of alleged 'contemnors'- 'respondents' and, therefore, contempt application was dismissed.

Delegation of Powers [Section 426]

The Tribunal or the Appellate Tribunal may, by general or special order, direct, subject to such conditions, if any, as may be specified in the order, any of its officers or employees or any other person authorized by it to inquire into any matter connected with any proceeding or, as the case may be, appeal before it and to report to it in such manner as may be specified in the order.

Protection of Action Taken in Good Faith [Section 428]

No suit, prosecution or other legal proceeding shall lie against the Tribunal, the President, Member, officer or other employee, or against the Appellate Tribunal, the Chairperson, Member, officer or other employees thereof or liquidator or any other person authorized by the Tribunal or the Appellate Tribunal for the discharge of any function under this Act in respect of any loss or damage caused or likely to be caused by any act which is in good faith done or intended to be done in pursuance of this Act.

Power to Seek Assistance of Chief Metropolitan Magistrate, Etc. [Section 429]

1. **Request for custody or control on property, book of accounts or other documents:** The Tribunal may, in **any proceedings for winding up** of a company under this Act or in **any proceedings under the Insolvency and Bankruptcy Code, 2016**, in order to take into custody or under its control all property, books of account or other documents, **request, in writing**, the Chief Metropolitan Magistrate, Chief Judicial Magistrate or the District Collector within whose jurisdiction any such property, books of account or other documents of such company under this Act or of corporate persons under the said Code, are situated or found, to take possession thereof, and the Chief Metropolitan Magistrate, Chief Judicial Magistrate or the District Collector, as the case may be, shall, on such request being made to him,—

- (a) take possession of such property, books of account or other documents; and
 - (b) cause the same to be entrusted to the Tribunal or other persons authorised by it.
- (2) **May act, as may necessary for securing compliance:** For the purpose of securing compliance with the provisions of sub-section (1), the Chief Metropolitan Magistrate, Chief Judicial Magistrate or the District Collector may take or cause to be taken such steps and use or cause to be used such force as may, in his opinion, be necessary.
- (3) **No act to be called in question:** No act of the Chief Metropolitan Magistrate, Chief Judicial Magistrate or the District Collector done in pursuance of this section shall be called in question in any court or before any authority on any ground whatsoever.

Civil Court Not to Have Jurisdiction [Section 430]

No civil court shall have jurisdiction to entertain any suit or proceeding in respect of any matter which the Tribunal or the Appellate Tribunal is empowered to determine by or under this Act or any other law for the time being in force and no injunction shall be granted by any court or other authority in respect of any action taken or to be taken in pursuance of any power conferred by or under this Act or any other law for the time being in force, by the Tribunal or the Appellate Tribunal.

Vacancy in Tribunal or Appellate Tribunal not to Invalidate Acts or Proceedings [Section 431]

No act or proceeding of the Tribunal or the Appellate Tribunal shall be questioned or shall be invalid merely on the ground of the existence of any vacancy or defect in the constitution of the Tribunal or the Appellate Tribunal, as the case may be.

Example 3: NCLT passed an order against Amma Ltd. on March 30, 2020. Amma Ltd. filed an Appeal with NCLAT on April 01, 2020, on the ground that the NCLT is not properly constituted according to the provisions of Companies Act, 2013. As per section 431 of the Companies Act, 2013, the company shall not question the proceeding of the tribunal on this ground.

Right to Legal Representation [Section 432]

A party to any proceeding or appeal before the Tribunal or the Appellate Tribunal, as the case may be, may either appear in person or authorize one or more Chartered Accountants or Company Secretaries or Cost Accountants or Legal Practitioners or any other person to present his case before the Tribunal or the Appellate Tribunal, as the case may be.

Limitation [Section 433]

The provisions of the Limitation Act, 1963 shall, as far as may be, apply to proceedings or appeals before the Tribunal or the Appellate Tribunal, as the case may be.

Transfer of Certain Pending Proceedings [Section 434]

- (1) On such date as may be notified by the Central Government in this behalf, —

- (a) **all matters, proceedings or cases pending before the Board of Company Law Administration** (herein in this section referred to as the Company Law Board) constituted under the Companies Act, 1956, immediately before such date shall stand transferred to the Tribunal and the Tribunal shall dispose of such matters, proceedings or cases in accordance with the provisions of this Act;
- (b) **any person aggrieved by any decision or order of the Company Law Board** made before such date may file an appeal to the High Court within 60 days from the date of communication of the decision or order of the Company Law Board to him on any question of law arising out of such order:

Provided that the High Court may if it is satisfied that the appellant was prevented by sufficient cause from filing an appeal within the said period, allow it to be filed within a further period not exceeding 60 days; and

- (c) **all proceedings** under the Companies Act, 1956, including proceedings relating to arbitration, compromise, arrangements and reconstruction and winding up of companies, pending immediately before such date before any District Court or High Court, shall stand transferred to the Tribunal and the Tribunal may proceed to deal with such proceedings from the stage before their transfer:

Provided further that any party or parties to any proceedings relating to the winding up of companies pending before any Court immediately before the commencement of the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2018, may file an application for transfer of such proceedings and the Court may by order transfer such proceedings to the Tribunal and the proceedings so transferred shall be dealt with by the Tribunal as an application for initiation of corporate insolvency resolution process under the Insolvency and Bankruptcy Code, 2016 .

Provided that only such proceedings relating to the winding up of companies shall be transferred to the Tribunal that are at a stage as may be prescribed by the Central Government.

Provided also that **only such proceedings relating to cases other than winding-up**, for which orders for allowing or otherwise of the proceedings are not reserved by the High Courts shall be transferred to the Tribunal:

Provided further that –

- (i) all proceedings under the Companies Act, 1956 other than the cases relating to winding up of companies that are reserved for orders for allowing or otherwise such proceedings: or
- (ii) the proceedings relating to winding up of companies which have not been transferred from the High Courts.

shall be dealt with in accordance with provisions of the Companies Act, 1956 and the Companies (Court) Rules, 1959.

Provided also that **proceedings relating to cases of voluntary winding up of a company** where notice of the resolution by advertisement has been given under sub-section (1) of section 485 of the Companies Act, 1956 but the company has not been dissolved before the 1st April, 2017 shall continue to be dealt with in accordance with provisions of the Companies Act, 1956 and the Companies (Court) Rules, 1959.

- (2) The **Central Government may make rules** consistent with the provisions of this Act to **ensure timely transfer of all matters, proceedings or cases pending** before the Company Law Board or the courts, to the Tribunal under this section.

In Union Bank of India v. Nilkamal Ltd. IA No. 3 of 2021 Co. Pet. No. 1 of 2015, January 27, 2022, is decided in view of the Insolvency and Bankruptcy Code (Second Amendment) Act, 2018, there can be no doubt when a party applies even in a pending case seeking winding-up it is obligatory on part of the High Court or any other Courts before whom the proceedings are pending to remit the matter to the Tribunal. It would be pertinent to note herein that when the order dated 21st March 2017 was passed rejecting the application for transfer, at that stage, The Insolvency and Bankruptcy Code (second Amendment) Act, 2018 was not available for consideration. Pursuant to 2018 amendment, the present application can be filed by respondent-Union Bank of India. Therefore, it was held that, when a party applies even in a pending case seeking winding up, it is obligatory on part of High Court or any other Courts before whom proceedings are pending to remit matter to NCLT.

3. SPECIAL COURT [SECTION 435-438]

Establishment of Special Court [Section 435]

Section 435 of the Companies Act deals with the establishment of the Special Court. The provisions state the number of special court that may be established with the required number of judges for the working.

Establishment of number of special court: The Central Government may by notification-

- for the purpose of providing speedy trial of offences under this Act **except under section 452**, establish or designate as many Special Courts as may be necessary.

Composition: A Special Court shall consist of—

(a) a single judge holding office as Session Judge or Additional Session Judge	→ in case of offences punishable under this Act with imprisonment of two years or more; and
(b) a Metropolitan Magistrate or a Judicial Magistrate of the First Class	→ in the case of other offences

Appointment: They shall be appointed by the Central Government with the concurrence of the Chief Justice of the High Court within whose jurisdiction the judge to be appointed is working.

Offences Triable by Special Courts [Section 436]

- (1) **Powers of special courts with respect to trial of offences:** Notwithstanding anything contained in the Code of Criminal Procedure (Cr. P. C), 1973, —

Powers of the special courts	Provisions
Offences that are triable by the special court	All offences specified under section 435(1) shall be triable only by the Special Court established for the area in which the registered office of the company in relation to which the offence is committed.
In case of more than one Special Courts	Where there are more Special Courts than one for such area, by such one of them as may be specified in this behalf by the High Court concerned;
Where a person accused of, or suspected of the commission of, an offence under this Act	Such person is forwarded to a Magistrate under section 167 of the Code of Criminal Procedure, 1973. (i) such Magistrate may authorize the detention of such person in such custody as he thinks fit for a period not exceeding fifteen days in the whole where such Magistrate is a Judicial Magistrate, (ii) and seven days in the whole where such Magistrate is an Executive Magistrate: Provided that where such Magistrate considers that the detention of such person (upon or before the expiry of the period of detention) is unnecessary, he shall order such person to be forwarded to the Special Court having jurisdiction;

Vested with same power as provided under the Cr. P.C	the Special Court may exercise the same power which a Magistrate having jurisdiction to try a case may exercise under section 167 of the Code of Criminal Procedure, 1973 in relation to an accused person who has been forwarded to him under that section;
Cognizance of offence by special court	A Special Court may, upon perusal of the police report of the facts constituting an offence under this Act or upon a complaint in that behalf, take cognizance of that offence without the accused being committed to it for trial.

- (2) **Special Court to try an offence other than an offence under this Act:** When trying an offence under this Act, a Special Court **may also try** an offence other than an offence under this Act with which the accused may, under the Code of Criminal Procedure, 1973 be charged at the same trial.
- (3) **Summary Trial:** Notwithstanding anything contained in the Code of Criminal Procedure, 1973,

Power of special court on summary trial of an offence	Nature of summary trial
The Special Court may, if it thinks fit, try in a summary way any offence under this Act	Which is punishable with imprisonment for a term not exceeding three years
In the case of conviction in a summary trial	no sentence of imprisonment for a term exceeding one year shall be passed
When at the commencement of, or in the course of, a summary trial, it appears to the Special Court that – - the nature of the case is such that the sentence of imprisonment for a term exceeding one year may have to be passed, or - that it is, for any other reason, undesirable to try the case summarily	the Special Court shall, after hearing the parties, record an order to that effect and thereafter recall any witnesses who may have been examined and proceed to hear or rehear the case in accordance with the procedure for the regular trial .

Appeal and Revision [Section 437]

The **High Court** may exercise, so far as may be applicable, all the powers conferred by Chapters XXIX and XXX which deals with **Appeals, Reference and Revision** of the Code of Criminal Procedure, 1973 on a High Court-

As if a **Special Court within the local limits of the jurisdiction of the High Court** were a Court of Session trying cases within the local limits of the jurisdiction of the High Court.

Application of Code to Proceedings before Special Court [Section 438]

Save as otherwise provided in this Act, the provisions of the Code of Criminal Procedure, 1973 shall apply to the proceedings before a Special Court and for the purposes of the said provisions, the Special Court shall be deemed to be a Court of Session or the court of Metropolitan Magistrate or a Judicial Magistrate of the First Class, as the case may be, and the person conducting a prosecution before a Special Court shall be deemed to be a Public Prosecutor.

4. OFFENCES TO BE NON-COGNIZABLE [SECTION 439]

This section provides of the offences that are non-cognizable. According to this section:

Nature of Offences	Consequences
Every offence under the Companies Act, 2013 except the offences referred to section 212(6)	shall be deemed to be non-cognizable within the meaning of the Cr.P.C
Court shall take cognizance of any offence under the Companies Act which is alleged to have been committed by any company or any officer thereof	Only on the written complaint of the Registrar, a shareholder or a member of the company, or of a person authorized by the Central Government in that behalf. [Section 439(2)]
W.r.t. cognizance of offences relating to issue and transfer of securities and non-payment of dividend	The court may, on a complaint in writing by a person authorized by the Securities and Exchange Board of India, take cognizance [Section 439(2)]
Non-applicability of section 439(2)	To a prosecution by a company of any of its officers
Where the complainant is the Registrar or a person authorized by the Central Government	The presence of such officer before the Court trying the offences shall not be necessary unless the court requires his personal attendance at the trial [Section 439(3)]
Non-applicability of section 439(2)	To any action taken by the liquidator of a company in respect of any offence alleged to have been committed in respect of any of the matters in Chapter XX (Winding up) or in any

	other provision of this Act relating to winding up of companies. The liquidator of a company shall not be deemed to be an officer of the company. [Section 439(4)]

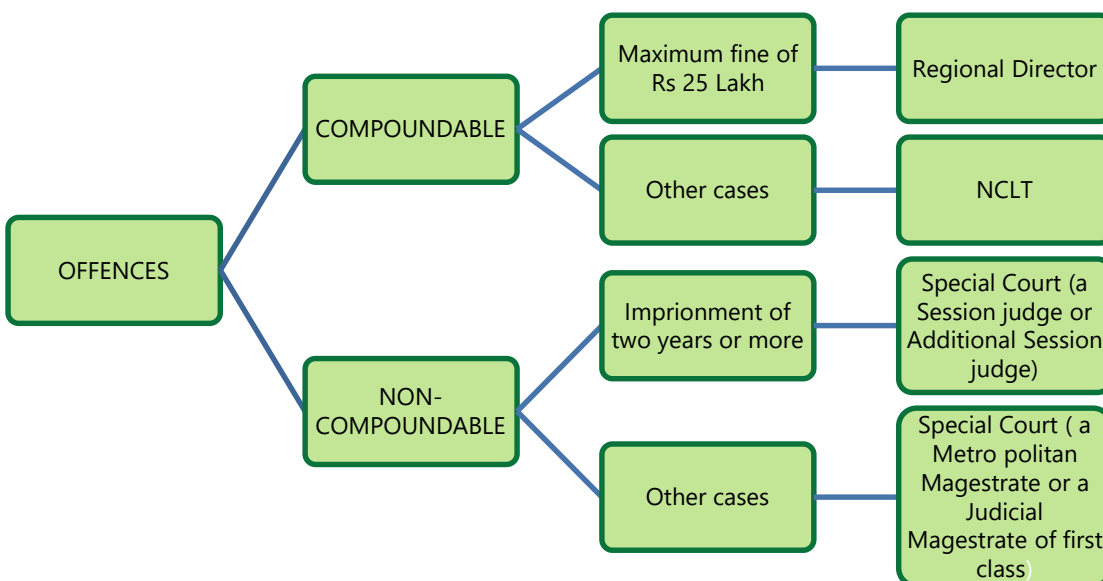
*As per the Notification G.S.R. 463(E) dated 5th June 2015, in case of a **government companies**, court shall take cognizance of an offence under this Act which is alleged to have been committed by any company or any officer thereof on the complaint in writing of a person authorized by the Central Government in that behalf.*

Explanation: Cognizable offence means an offence in which a police officer has the authority to make an arrest without a warrant and to start an investigation with or without the permission of a court. Cognizable offences are usually those offences which are serious in nature.

Whereas non-cognizable offence means an offence for which, and 'non-cognizable case' means a case in which, a police officer without any warrant has no authority to arrest.



5. COMPOUNDING OF CERTAIN OFFENCES [SECTION 441]



- (1) **Compounding of offences:** Notwithstanding anything contained in the Code of Criminal Procedure, 1973 any offence punishable under this Act (whether committed by a company or any officer thereof) not being an offence punishable with imprisonment only, or punishable with imprisonment and also with fine, may, either before or after the institution of any prosecution, be compounded by—

- (a) the **Tribunal**; or
- (b) where the maximum amount of fine which may be imposed for such offence does not exceed twenty-five lakh rupees, **by the Regional Director** or **any officer** authorized by the Central Government,

-on payment or credit, by the company or, as the case may be, the officer, to the Central Government of such sum as that Tribunal or the Regional Director or any officer authorized by the Central Government, as the case may be, may specify:

Provided that the sum so specified shall not, in any case, exceed the maximum amount of the fine which may be imposed for the offence so compounded:

Payment of sum by way of additional fee: **Provided further** that in specifying the sum required to be paid or credited for the compounding of an offence under this sub-section, the sum, if any, paid by way of additional fee under sub-section (2) of section 403 shall be taken into account.

Exception : **Provided also** that any offence covered under this sub-section by any company or its officer **shall not be compounded** if the investigation against such company has been initiated or is pending under this Act.

- (2) **Non-Applicability of Sub-section (1):** Nothing in sub-section (1) shall apply to an offence committed by a company or its officer **within a period of three years** from the date on which a similar offence committed by it or him was compounded under this section.

Explanation—For the purposes of this section, —

- (a) **any second or subsequent offence committed after the expiry of a period of three years** from the date on which the offence was previously compounded, shall be deemed to be a first offence;
- (b) **"Regional Director"** means a person appointed by the Central Government as a Regional Director for the purposes of this Act.

- (3) **Filing of an application for compounding :**

- (a) Every application for the compounding of an offence shall be made to the Registrar who shall forward the same, together with his comments thereon, **to the Tribunal or the Regional Director or any officer** authorized by the Central Government, as the case may be.
- (b) **Intimation of compounding:** Where any offence is compounded under this section, whether before or after the institution of any prosecution, an intimation thereof shall

be given by the company **to the Registrar within seven days** from the date on which the offence is so compounded.

(c) **When no prosecution to be instituted:**

(i) **Where any offence is compounded before the institution of any prosecution**, no prosecution shall be instituted in relation to such offence, either by the Registrar or by any shareholder of the company or by any person authorized by the Central Government against the offender in relation to whom the offence is so compounded.

(ii) **Where the compounding of any offence is made after the institution of any prosecution**, such compounding shall be brought by the Registrar in writing, to the notice of the court in which the prosecution is pending and on such notice of the compounding of the offence being given, the company or its officer in relation to whom the offence is so compounded shall be discharged.

(4) **File or register return, account or other document :** The Tribunal or the Regional Director or any officer authorized by the Central Government, as the case may be, while dealing with a proposal for the compounding of an offence for a default in compliance with any provision of this Act which requires a company or its officer to file or register with, or deliver or send to, the Registrar any return, account or other document, may direct, by an order, if it or he thinks fit to do so, any officer or other employee of the company to file or register with, or on payment of the fee, and the additional fee, required to be paid under section 403, such return, account or other document within such time as may be specified in the order.

(5) **In case of contravention of an order:** If any officer or other employee of the company who fails to comply with any order made by the Tribunal or the Regional Director or any officer authorized by the Central Government under sub-section (4), the **maximum amount of fine** for the offence proposed to be compounded under this section **shall be twice the amount** provided in the corresponding section in which punishment for such offence is provided.

(6) **Offences which cannot be compounded:** Notwithstanding anything contained in the Code of Criminal Procedure, 1973, any offence which is punishable under this Act with imprisonment only or with imprisonment and also with fine shall not be compoundable.

(7) No offence specified in this section shall be compounded except under and in accordance with the provisions of this section.

Process for compounding of an offence-

- Filing of an application to Registrar
- he will forward with his comments to Tribunal/RD/Officer authorised by CG
- Tribunal/RD/Officer may direct, by an order, any officer or other employee of the company
- to file or register with return, account or other document within such time as may be specified
- If any officer or other employee of the company who fails to comply with any order -
- the **maximum amount of fine** for the offence proposed to be compounded **shall be twice the amount** provided in the corresponding section in which punishment for such offence is provided.



6. MEDIATION AND CONCILIATION PANEL [SECTION 442]

- (1) **Mediation and Conciliation Panel:** The **Central Government** shall maintain a panel of experts to be called as the Mediation and Conciliation Panel.

Composition: It shall be consisting of such number of experts having such qualifications as may be prescribed for mediation between the parties during the pendency of any proceedings before-

- the Central Government or
- the Tribunal or
- the Appellate Tribunal under this Act.

- (2) **Referring of matters by any parties to the proceedings to Mediation and Conciliation Panel:** Any of the parties to the proceedings may, at any time during the proceedings before the Central Government or the Tribunal or the Appellate Tribunal, apply to the Central Government or the Tribunal or the Appellate Tribunal, as the case may be, in such form along with such fees as may be prescribed, for referring the matter pertaining to such proceedings to the Mediation and Conciliation Panel and the Central Government or Tribunal or the Appellate Tribunal, as the case may be, shall appoint one or more experts from the panel referred to in sub-section (1).

- (3) **Suo moto referring of matters to Mediation and Conciliation Panel:** The Central Government or the Tribunal or the Appellate Tribunal before which any proceeding is pending may, Suo moto, refer any matter pertaining to such proceeding to such number of experts

from the Mediation and Conciliation Panel as the Central Government or the Tribunal or the Appellate Tribunal, as the case may be, deems fit.

- (4) **Fees and other conditions of experts:** The fee and other terms and conditions of experts of the Mediation and Conciliation Panel shall be such as may be prescribed.
- (5) **Procedure and disposal of matter:** The Mediation and Conciliation Panel shall follow such procedure as may be in Rule 11 and 19 of the *Companies (Mediation and Conciliation) Rules, 2016*, and dispose of the matter referred to it within a period of three months from the date of appointment of expert from the panel and forward its recommendations to the Central Government or the Tribunal or the Appellate Tribunal, as the case may be.
- (6) **Objection to the recommendation of the Mediation and Conciliation Panel:** Any party aggrieved by the recommendation of the Mediation and Conciliation Panel may file objections to the Central Government or the Tribunal or the Appellate Tribunal, as the case may be.



7. SERIOUS FRAUD INVESTIGATION OFFICE [SECTION 211& 212]

Establishment of Serious Fraud Investigation Office (SFIO)

The Central Government shall, by notification, establish an office to be called the Serious Fraud Investigation Office to investigate frauds relating to a company.

Composition : The Serious Fraud Investigation Office shall be headed by a Director and consist of such number of experts from the different fields to be appointed by the Central Government from amongst persons of ability, integrity and experience in banking, corporate affairs, taxation, capital market etc.

Function of SFIO: where the Central Government is of the opinion, that it is necessary to investigate into the affairs of a company by the Serious Fraud Investigation Office—

- (a) on receipt of a report of the Registrar or inspector under section 208;
- (b) on intimation of a special resolution passed by a company that its affairs are required to be investigated;
- (c) in the public interest; or
- (d) on request from any Department of the Central Government or a State Government,

The Central Government may, by order, assign the investigation into the affairs of the said company to the Serious Fraud Investigation Office and its Director, may designate such number of inspectors, as he may consider necessary for the purpose of such investigation.

[For detail, refer chapter of Inspection, Inquiry and Investigation]



8. POWER OF CENTRAL GOVERNMENT TO APPOINT COMPANY PROSECUTORS [SECTION 443]

The Central Government may **appoint one or more persons**, as company prosecutors for the conduct of prosecutions arising out of this Act, generally, or for any case, or in any case, or for any specified class of cases in any local area.

The persons so appointed as company prosecutors shall have **all the powers and privileges conferred by the Code** on Public Prosecutors appointed under section 24 of the Code.



9. APPEAL AGAINST ACQUITTAL [SECTION 444]

The Central Government may, in any case arising under this Act, direct any-

- company prosecutor or
- authorize any other person either by name or by virtue of his office,

to present an appeal from an order of acquittal passed by any court, other than a High Court, and an appeal presented by such prosecutor or other person shall be deemed to have been validly presented to the appellate court.



10. COMPENSATION FOR ACCUSATION WITHOUT REASONABLE CAUSE [SECTION 445]

The provisions of section 250 of the Code of Criminal Procedure, 1973 shall apply *mutatis mutandis* to compensation for accusation without reasonable cause before the Special Court or the Court of Session.



11. APPLICATION OF FINES [SECTION 446]

According to this section, the court imposing any fine under this Act may direct that the whole or any part thereof shall be applied in or towards payment of the costs of the proceedings, or in or towards the payment of a reward to the person on whose information the proceedings were instituted.



12. FACTORS FOR DETERMINING LEVEL OF PUNISHMENT [SECTION 446A]

According to this section, the Court or the Special Court, while deciding the amount of fine or imprisonment under this Act, shall have due regard to the following factors, namely: —

- (a) size of the company.
- (b) nature of business carried on by the company.
- (c) injury to public interest.
- (d) nature of the default; and
- (e) repetition of the default.



13. LESSER PENALTIES FOR ONE PERSON COMPANIES OR SMALL COMPANIES [SECTION 446B]

According to this section, notwithstanding anything contained in this Act, if penalty is payable for non-compliance of any of the provisions of this Act by a One Person Company, small company, start-up company or Producer Company, or by any of its officer in default, or any other person in respect of such company, then such company, its officer in default or any other person, as the case may be, shall be liable to a penalty which shall not be more than one-half of the penalty specified in such provisions subject to a maximum of two lakh rupees in case of a company and one lakh rupees in case of an officer who is in default or any other person, as the case may be.

Explanation. —For the purposes of this section-

- (a) "Producer Company" means a company as defined in clause (l) of section 378A;
- (b) "start-up company" means a private company incorporated under this Act or under the Companies Act, 1956 and recognized as start-up in accordance with the notification issued by the Central Government in the Department for Promotion of Industry and Internal Trade.



14. ADJUDICATION OF PENALTIES [SECTION 454]

- (1) The Central Government may, by an order published in the Official Gazette, appoint as many officers of the Central Government, not below the rank of Registrar, as adjudicating officers for adjudging penalty under the provisions of this Act in the manner as provided in Rule 3 of the Companies(Adjudication of Penalties) Rules, 2014.

Manner of adjudication of Penalties [Rule 3 of the Companies (Adjudication of Penalties) Rules, 2014]

- (i) **Appointment of Adjudicating officers:** The Central Government may appoint any of its officers, not below the rank of Registrar, as adjudicating officers for adjudging penalty under the provisions of the Act.
- (ii) **Issue of written notice by an adjudicating officer:** Before adjudging penalty, the adjudicating officer shall issue a written notice in the specified manner-
 - to the company and

- to officer of the company who is in default or
- any other person, as the case may be.

to show cause, within such period as may be specified in the notice (not being less than fifteen days and more than thirty days from the date of service thereon), why the penalty should not be imposed on it or him.

- (iii) **Manner of the written notice:** Every notice issued above shall clearly indicate the nature of non-compliance or default under the Act alleged to have been committed or made by

- such company,
- officer in default, or
- any other person, as the case may be.

and also draw attention to the relevant penal provisions of the Act and the maximum penalty which can be imposed on the company, and each of the officers in default, or the other person.

- (iv) **Period of filing reply to the notice:** The reply to such notice shall be filed in electronic mode only within the period as specified in the notice:

Provided that the adjudicating officer may, for reasons to be recorded in writing, extend the period referred to above by a further period not exceeding fifteen days, if the company or officer in default or any person as the case may be, satisfies the adjudicating officer that it or he has sufficient cause for not responding to the notice within the stipulated period or the adjudicating officer has reason to believe that the company or the officer or the person has received a shorter notice and did not have reasonable time to give reply.

- (v) **Physical appearance:** If, after considering the reply submitted by such company, its officer, or any other person, as the case may be, the adjudicating officer is of the opinion that physical appearance is required, he shall issue a notice, within a period of ten working days from the date of receipt of reply fixing a date for the appearance of such company, through its authorised representative, or officer of such company, or any other person, whether personally or through his authorised representative.

Provided that if any person, to whom a notice is issued under point (ii), desires to make an oral representation, whether personally or through his authorised representative and has indicated the same while submitting his reply in electronic mode, the adjudicating officer shall allow such person to make such representation after fixing a date of appearance.

- (vi) **Passing of an order by the adjudicating officer:** On the date fixed for hearing and after giving a reasonable opportunity of being heard to the person concerned, the adjudicating officer may, subject to reasons to be recorded in writing, pass any order in writing as he thinks fit including an order for adjournment.

Provided that after hearing, adjudicating officer may require the concerned person to submit his reply in writing on certain other issues related to the notice under point (ii) relevant for determination of the default.

- (vii) **Period for passing the order:** The adjudicating officer shall pass an order:
- (a) within 30 days of the expiry of the period referred in point (ii) or of such extended period as referred therein, where physical appearance was not required under point (v).
 - (b) within 90 days of the date of issue of notice under point (ii), where any person appeared before the adjudicating officer under point (v):

However, in case an order is passed after the aforementioned duration, the reasons of the delay shall be recorded by the adjudicating officer and no such order shall be invalid merely because of its passing after the expiry of such 30 days or 90 days as the case may be.

- (viii) **Date and sign on order:** Every order of the adjudicating officer shall be duly dated and signed by him and shall clearly state the reasons for requiring the physical appearance under point (v).
- (ix) **Forwarding of copy of an order:** The adjudicating officer shall send a copy of the order passed by him
- to the concerned company,
 - officer who is in default or
 - any other person or
 - all of them and
 - to the Central Government and
 - a copy of the order shall also be uploaded on the website.
- (x) **Powers of Adjudicating Authority:** For the purposes of this rule , the adjudicating officer shall have the following powers, namely:-
- (a) to summon and enforce the attendance of any person acquainted with the facts and circumstances of the case after recording reasons in writing;
 - (b) to order for evidence or to produce any document, which in the opinion of the adjudicating officer, may be relevant to the subject matter.
- (xi) **Failure to be present before the adjudicating authority:** If any person fails to reply or neglects or refuses to appear as required under point (v) or point (x) before the adjudicating officer, the adjudicating officer may pass an order imposing the penalty, in the absence of such person after recording the reasons for doing so.
- (xii) **Consideration to following factors while levying penalty:** While adjudging quantum of penalty, the adjudicating officer shall have due regard to the following factors, namely: -

- (a) size of the company.
- (b) nature of business carried on by the company:
- (c) injury to public interest.
- (d) nature of the default.
- (e) repetition of the default.
- (f) the amount of disproportionate gain or unfair advantage, wherever quantifiable, made as a result of the default; and
- (g) the amount of loss caused to an investor or group of investors or creditors as a result of the default:

However, in no case, the penalty imposed shall be less than the minimum penalty prescribed, if any, under the relevant section of the Act.

- (xiii) **Fixed sum of penalty:** In case a fixed sum of penalty is provided for default of a provision, the adjudicating officer shall impose that fixed sum, in case of any default therein.
- (xiv) **Payment of penalty:** Penalty shall be paid through Ministry of Corporate Affairs portal only.
- (xv) **Sum to be credited to the Consolidated Fund of India:** All sums realised by way of penalties under the Act shall be credited to the Consolidated Fund of India.

*Explanation: For the purposes of this rule, the term “specified manner” shall mean service of documents as specified under section 20 of the Act and the rules made

thereunder and details in respect of address (including electronic mail ID) provided in the KYC documents filed in the registry shall be used for communication under this Rule.

- (2) The Central Government shall while appointing adjudicating officers, specify their jurisdiction in the order under sub-section (1).
- (3) The adjudicating officer may, by an order—
 - (a) impose the penalty on the company, the officer who is in default, or any other person, as the case may be, stating therein any non-compliance or default under the relevant provisions of this Act; and
 - (b) direct such company, or officer who is in default, or any other person, as the case may be, to rectify the default, wherever he considers fit.

Provided that in case the default relates to non-compliance of sub-section (4) of section 92 or sub-section (1) or sub-section (2) of section 137 and such default has been rectified either prior to, or within thirty days of, the issue of the notice by the adjudicating officer, no penalty shall be imposed in this regard and all proceedings under this section in respect of such default shall be deemed to be concluded.

- (4) The adjudicating officer shall, before imposing any penalty, give a reasonable opportunity of being heard to such company, the officer who is in default or any other person.
- (5) Any person aggrieved by an order made by the adjudicating officer may prefer an appeal to the Regional Director having jurisdiction in the matter.
- (6) Every appeal shall be filed within sixty days from the date on which the copy of the order made by the adjudicating officer is received by the aggrieved person and shall be in such form, manner and be accompanied by such fees in Rule 4 of the Companies (Adjudication of Penalties) Rules, 2014.
- (7) The Regional Director may, after giving the parties to the appeal an opportunity of being heard, pass such order as he thinks fit, confirming, modifying or setting aside the order appealed against.
- (8) (i) Where **company** fails to comply with the order made under sub-section (3) or sub-section (7), as the case may be within a period of ninety days from the date of the receipt of the copy of the order, the company shall be punishable with fine which shall not be less than twenty five thousand rupees but which may extend to five lakh rupees.
- (ii) Where **an officer of a company or any other person** who is in default fails to comply with the order made under sub-section (3) or sub-section (7), as the case may be, within a period of ninety days from the date of the receipt of the copy of the order, such officer shall be punishable with imprisonment which may extend to six months or with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees, or with both.



15. PENALTY FOR REPEATED DEFAULT [SECTION 454A]

Where a company or an officer of a company or any other person having already been subjected to penalty for default under any provisions of this Act, **again commits such default within a period of three years** from the date of order imposing such penalty passed by the adjudicating officer or the Regional Director, as the case may be, it or he **shall be liable for the second or subsequent defaults** for an amount equal to twice the amount of penalty provided for such default under the relevant provisions of this Act.

TEST YOUR KNOWLEDGE**Multiple Choice Questions**

1. As per the Companies Act, 2013, every petition filed before the Tribunal shall be disposed of:
 - (a) within 1 month from the date application is admitted
 - (b) within 2 months from the date of first hearing
 - (c) within 3 months from the date of its presentation
 - (d) within 6 months from its filing
2. Trial of an offence under the Companies Act, by special court shall be of such an offence:
 - (a) which is punishable with imprisonment for a term exceeding one year
 - (b) which is punishable with imprisonment for a term not exceeding one year
 - (c) which is punishable with imprisonment for a term exceeding three years
 - (d) which is punishable with imprisonment for a term not exceeding three years
3. Makhija Developers Limited, being unsatisfied with the order given by the NCLT, desires to prefer an appeal against the order of the NCLT. You, as a legal advisor to Makhija Developers Limited, are required to provide them with the best course of action available considering the provisions of the Companies Act, 2013.
 - (a) Makhija Developers Limited cannot prefer an appeal against an order passed by NCLT Mumbai u/s 9 of the Insolvency and Bankruptcy Code as Interim Resolution Professional is already appointed.
 - (b) Makhija Developers Limited may be able to prefer an appeal against the order passed by NCLT Mumbai within a period of 45 days from the date of order of copy made available to Makhija Developers Limited.
 - (c) Makhija Developers Limited cannot prefer an appeal against an order passed by NCLT Mumbai u/s 9 of the Insolvency and Bankruptcy Code as reasonable opportunity of being heard was given to Makhija Developers Limited.
 - (d) Makhija Developers Limited may be able to prefer an appeal against the order passed by NCLT Mumbai within a period of 60 days from the date of order of copy made available to Makhija Developers Limited.
4. Requisite number of shareholders of Vimaan Aerospace Limited, which has been incorporated under the Companies Act, 2013, filed an application with the National Company Law Tribunal (NCLT) under Section 241 highlighting the mismanagement in the conduct of the affairs of the company. Taking cognizance of the application, the National Company Law

Tribunal (NCLT) passed an order under Section 420 on November 23, 2021, providing the sought after relief to the shareholders of Vimaan Aerospace Limited. On finding some mistake in the order, the shareholders brought the same to the notice of NCLT for rectification. You are required to select the correct statement from those given below as to the circumstances under which NCLT would be able to amend its order and the maximum period which the said order can be amended:

- (a) National Company Law Tribunal (NCLT) can amend its order to rectify any mistake apparent from the record when such mistake is brought to its notice by the parties and further, the order can be amended by NCLT at any time within a period of six months from the date of such order provided no appeal has been made against the said order.
- (b) National Company Law Tribunal (NCLT) can amend its order to rectify any mistake apparent from the record when such mistake is brought to its notice by the parties and further, the order can be amended by NCLT at any time within a period of one year from the date of such order provided no appeal has been made against the said order.
- (c) National Company Law Tribunal (NCLT) can amend its order to rectify any mistake apparent from the record when such mistake is brought to its notice by the parties and further, the order can be amended by NCLT at any time within a period of two years from the date of such order provided no appeal has been made against the said order.
- (d) National Company Law Tribunal (NCLT) can amend its order to rectify any mistake apparent from the record when such mistake is brought to its notice by the parties and further, the order can be amended by NCLT at any time within a period of three years from the date of such order provided no appeal has been made against the said order.

Descriptive Questions

1. In the annual general meeting of XYZ Ltd., while discussing on the matter of retirement and reappointment of director Mr. X, allegations of fraud and financial irregularities were levelled against him by some members. This resulted into chaos in the meeting. The situation was normal only after the Chairman declared about initiating an inquiry against the director. Mr. X, however, could not be re-appointed in the meeting. The matter was published in the newspapers next day. On the basis of such news, whether the court can take cognizance of the matter and take action against the director on its own?

Justify your answer with reference to the provisions of the Companies Act, 2013.

2. What is the object of Constituting Panel for Mediation and Conciliation under the Companies Act, 2013? Who can file application for mediation and conciliation?
3. Mr. Joseph, a member of Armaments Ltd., is aggrieved due to failure of the company to make payment of dividend declared in the AGM held in August 2015. He makes a complaint, in writing, before the court of competent jurisdiction within the prescribed period of limitation, but the court refused to take cognizance of the alleged offence. Explain the legal position in this regard under the Companies Act, 2013.

Also state the offences under the Companies Act, 2013 which are cognizable and which are non-cognizable.

4. Excel Ltd. committed an offence under the Companies Act, 2013. The offence falls within the jurisdiction of a special court of Bundi district in which the registered office of Excel Ltd was situated. However, in that Bundi district, there were two special courts one in X place and other in Y place. Identify the jurisdiction of special court for trial of an offence committed by Excel Ltd.
5. Before imposing penalty, the adjudicating authority issued a show cause notice to the company and its officers on 15th July, 2020 to represent before the adjudicating authority. The notice was served on them on 31st July 2020. State the time period within which the company and its officers who were called upon may be present before the Adjudicating authority.
6. On an application filed before Tribunal from one of the shareholder of Company, Tribunal (NCLT) passed order on 20th December 2019 without the consent of parties. Mr. Rama, one of the party to the proceeding whose family condition was not good so didn't take much interest in order of tribunal but after few days due to aggrieved by the order, he filed an appeal before Appellate Tribunal (NCLAT) on 15th March 2020 showing sufficient cause of delay for not filing appeal up to 45 days from the date of order. The Appellate Tribunal has passed an order dated 30th April 2020, Mr. Rama was not satisfied and made application to Supreme Court on 30th September 2020 against the order of the Appellate Tribunal.

Considering the given situation, examine whether Appeal filed before the Supreme Court is admissible after showing cause of delay.

ANSWER KEYS

Answer to Multiple Choice Questions

1.	C	2.	d	3.	b	4.	c

Descriptive Answers

1. Section 439 of the Companies Act, 2013 provides that offences under the Act shall be non-cognizable. As per this section:
 1. Notwithstanding anything contained in the Code of Criminal Procedure, 1973, every offence under this Act except the offences referred to in sub section (6) of section 212 shall be deemed to be non-cognizable within the meaning of the said Code.
 2. No court shall take cognizance of any offence under this Act which is alleged to have been committed by any company or any officer thereof, except on the complaint in writing of the Registrar, a shareholder or a member of the company, or of a person authorized by the Central Government in that behalf.

Thus, in the given situation, the court shall not initiate any *Suo moto* action against the director Mr. X without receiving any complaint in writing of the Registrar of Companies, a shareholder of the company or of a person authorized by the Central Government in this behalf.

2. Under section 442 of the Companies Act, 2013, it is provided that the Central Government shall maintain a panel of experts for mediation between the parties during pendency of any proceedings before the Central Government or the Tribunal or the Appellate Tribunal under the Act. In common parlance, mediation means intervention of some third party in a dispute with the intention to resolve the dispute. Similarly, conciliation means the powers of adjusting or settling disputes in a friendly manner through extra judicial means. The object behind the panel is to dispose the matter pending before the Government / Tribunal as mentioned above.

Filing of application: Application for mediation and conciliation can be made by:

- (A) any parties to the proceedings (It shall be accompanied with such fees and in such form as may be prescribed)
 - (B) The Central Government or the Tribunal or the Appellate Tribunal before which any proceeding is pending may, *Suo moto* refer any matter pertaining to such proceeding to such number of experts as it may deem fit.
3. **Cognizance of offence:** A court shall take cognizance of any offence under this Act which is alleged to have been committed by any company or any officer thereof only on the written complaint of -
 - (a) The Registrar,
 - (b) A shareholder of the company
 - (c) A member of the company, or
 - (d) Of a person authorised by the Central Government in that behalf.

Provided that the court may take cognizance of offences relating to issue and transfer of securities and non-payment of dividend, on a complaint in writing, by a person authorized by the Securities and Exchange Board of India.

In the present case, Mr. Joseph, a member of Armaments Ltd. is aggrieved due to failure of the company to make payment of dividend declared in the AGM held in August 2015. He makes a complaint, in writing, before the court of competent jurisdiction within the prescribed period of limitation, but the court refused to take cognizance of the alleged offence.

Here, the Court shall take cognizance of the offence relating to nonpayment of dividend as the shareholder have made a complaint in writing before the competent jurisdiction.

Cognizable and non-cognizable offences: Overriding the provisions given under the Code of Criminal Procedure, 1973, every offence under the Companies Act, 2013 except the offences referred to in section 212(6) of the Companies Act, 2013, which deals with the investigation into affairs of company by serious fraud investigation office, shall be deemed to be non-cognizable within the meaning of the said Code.

Therefore, the offences as covered under section 212(6) shall now be deemed to be cognizable where police officer may arrest person without warrant and are non-bailable. The Companies Act, 2013 establishes the offence covered under section 212(6) as a public wrong which has to be prevented and controlled. This non-bailable nature of the offences deter the offender and the others from committing further and similar offences.

4. All offences which are punishable in this Act with imprisonment of 2 years or more, shall be triable only by the special court established for the area in which the registered office of the company in relation to which the offence is committed. According to section 436 where there are more special courts than one for such area, by such one of them as may be specified in this behalf by the High court concerned.

Accordingly, in the given case, there are more than one special court in Bundi district where registered office of Excel Ltd. is situated. The jurisdiction for trial in special court will be specified by H.C of the State (i.e. Rajasthan).

5. **Issue of written notice by an adjudicating officer:** Rule 3 of the *Companies (Adjudication of Penalties) Rules, 2014* read with section 454 of the Companies Act, 2013, states that before adjudging penalty, the adjudicating officer shall issue a written notice in the specified manner-

- to the company and
- to officer of the company who is in default or
- any other person, as the case may be

to show cause, within such period as may be specified in the notice (not being less than fifteen days and more than thirty days from the date of service thereon), why the penalty should not be imposed on it or him.

Accordingly, the company and its officers shall be presented before the Adjudicating Authority on or before 30th August 2020 (being not more than 30 days from the date of service of notice thereon).

6. According to Section 423 of the Companies Act, 2013, any person aggrieved by an order of the Appellate Tribunal may prefer an appeal to the Supreme Court on any question of law arising out of Appellate Tribunal's order.

Every appeal shall be filed within a period of 60 days from the date on which a copy of the order of the Appellate Tribunal is made available to the person aggrieved and shall be in such form, and accompanied by such fees, as may be prescribed.

Supreme Court may entertain an appeal even after the expiry of the said period of 60 days from the date aforesaid, but within a further period not exceeding 60 Days, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within period.

In above case, since Mr. Rama even aggrieved by order of Appellate Tribunal filed application before Supreme Court on 30th September 2020. But as Supreme Court can entertain appeal only up to 60 days + 60 Days (Extension if sufficient cause). Since this appeal was filed beyond 120 days by Mr. Rama, so, appeal filed before the Supreme Court is not admissible.

[illegible]

CHAPTER

10

e-FILING



LEARNING OUTCOMES

At the end of this chapter, you will be able to:

- ☐ Know about MCA21
- ☐ Identify the applicable statutory provisions relating to e-Filing
- ☐ Understand the various e-Forms
- ☐ Elucidate the process involved in e-Filing
- ☐ Explain XBRL
- ☐ Know about fees payable for filing of documents, etc.



1. INTRODUCTION

The 'MCA21 e-Governance Project' is one of the Mission Mode Projects of the Government of India under the National e-Governance plans. It is developed to provide easy and secured on-line services through the use of information technology to various stakeholders. It was initially launched at Coimbatore as a Pilot Project on February 18, 2006 by Ministry of Corporate Affairs ("MCA"). The second Pilot Project was launched at Delhi on March 18, 2006. Thereafter, the project was launched in a progressive manner through India. The nationwide roll-out was completed across all the offices of twenty Registrars of Companies as on September 4, 2006.

The project is named MCA21 as it aims at repositioning MCA as an organisation capable of fulfilling the aspirations of its stakeholders in 21st Century.

The MCA21 application is designed to fully automate all processes related to the proactive enforcement and compliance of the legal requirements under the old Companies Act, 1956 and new Companies Act, 2013. This will help the business community to meet their statutory obligations.

e-Filing facility covers the Headquarters (at New Delhi), the offices of Registrar of Companies (RoCs) and of Regional Directors (RDs). Some of the e-filing facilities available at the MCA21 portal are as under:

- (a) Incorporation of new companies
- (b) Filing of Financial Statements and Annual Returns
- (c) Registration of charges
- (d) Verification, modification and satisfaction of charges
- (e) Event based statutory filings
- (f) Services related to Director Identification Number (DIN)
- (g) Inspection of documents and issue of certified copies
- (h) Approval from the Central Government
- (i) Approval from Regional Director (RD)
- (j) Approval from Registrar of Companies
- (k) Fees refund
- (l) Redressal of Investors' complaints

Some of the salient **features of MCA21** are as under:

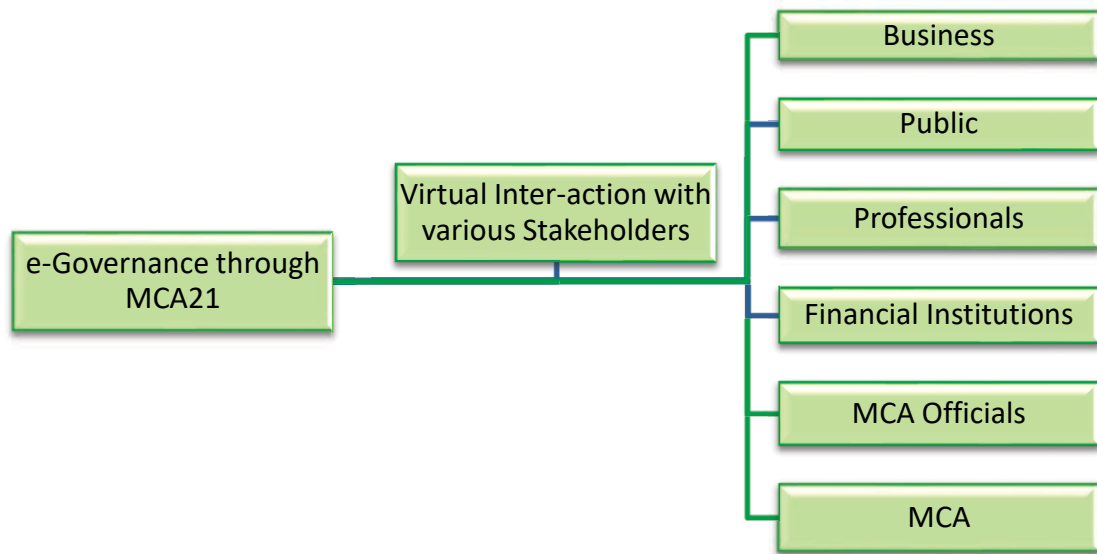
1. **Online Portal:** MCA21 is the online portal of the Ministry of Corporate Affairs (MCA). It has made all company related information accessible to various stakeholders and the general public.

2. *Convenient:* It provides the services on the basis of anywhere and anytime with speed and certainty.
3. *Easy and secure access:* It provides easy and secure access of the MCA services to various stakeholders.
4. *Full Automation:* It has fully automated all the processes, thus making India globally competitive.
5. *Multiple Payment Options:* It provides multiple options to make online payment.
6. *SRN:* It provides Service Request Number (SRN) which enables the stakeholders to track their service request.

Features of MCA21					
Online Portal of the Ministry of Corporate Affairs (MCA)	Convenient	Easy and secure access of the MCA services	Full automation of all the processes	Multiple options for payment	Provides SRN

MCA21 has made all company related information accessible to various stakeholders, which are as under:

1. **Business:** MCA21 has enabled business community to register a company and file statutory documents quickly and easily.
2. **Public:** The general public can get easy access to relevant records and get their grievances redressed effectively.
3. **Professionals:** The professionals like Chartered Accountants, Cost Accountants, Company Secretaries, Advocates, etc. are able to offer efficient services to their client companies.
4. **Financial Institutions:** Various financial institutions like banks, NBFCs, etc. can easily register, modify and verify the charges.
5. **MCA Officials:** MCA21 enables the MCA officials to deliver best services to various stakeholders. It gives more time and data to them for monitoring and supervision.
6. **MCA:** MCA21 enables the Ministry of Corporate Affairs to play its regulatory role in a more effective and transparent manner.



The MCA21 application offers the following **benefits**:

1. Enables the business community to register a company and file statutory documents quickly and easily.
2. Provides easy access of public documents
3. Helps faster and effective resolution of public grievances
4. Helps registration and verification of charges easily
5. Ensures proactive and effective compliance with relevant laws and corporate governance
6. Enables the MCA employees to deliver best of breed services

it is noteworthy that the concept of e-governance has been given statutory recognition through sections 398 and sections 400 to 402 of the Companies Act, 2013 read with Rules 7 and 8 of the Companies (Registration Offices and Fees) Rules, 2014.

2. PROVISIONS RELATING TO FILING OF APPLICATIONS, DOCUMENTS, INSPECTION, ETC., IN ELECTRONIC FORM [SECTION 398]

Section 398 of the Companies Act, 2013 relates to making of rules by the Central Government for enabling e-filing of various forms.

Sub-section (1) states that notwithstanding anything to the contrary contained in this Act, and without prejudice to the provisions contained in section 6 of the Information Technology Act, 2000, the

Central Government may make rules so as to require from such date as may be prescribed in the rules that—

- (a) such applications, balance sheet, prospectus, return, declaration, memorandum, articles, particulars of charges, or any other particulars or document as may be required to be filed or delivered under this Act or the rules made thereunder, shall be filed in the electronic form and authenticated in such manner as may be prescribed;
- (b) such document, notice, any communication or intimation, as may be required to be served or delivered under this Act, in the electronic form and authenticated in such manner as may be prescribed;
- (c) such applications, balance sheet, prospectus, return, register, memorandum, articles, particulars of charges, or any other particulars or document and return filed under this Act or rules made thereunder shall be maintained by the Registrar in the electronic form and registered or authenticated, as the case may be, in such manner as may be prescribed;
- (d) such inspection of the memorandum, articles, register, index, balance sheet, return or any other particulars or document maintained in the electronic form, as is otherwise available for inspection under this Act or the rules made thereunder, may be made by any person through the electronic form in such manner as may be prescribed;
- (e) such fees, charges or other sums payable under this Act or the rules made thereunder shall be paid through the electronic form and in such manner as may be prescribed; and
- (f) the Registrar shall register change of registered office, alteration of memorandum or articles, issue certificate of incorporation, register such document, issue such certificate, record the notice, receive such communication as may be required to be registered or issued or recorded or received, as the case may be, under this Act or the rules made thereunder or perform duties or discharge functions or exercise powers under this Act or the rules made thereunder or do any act which is by this Act directed to be performed or discharged or exercised or done by the Registrar in the electronic form in such manner as may be prescribed.

Explanation.— For the removal of doubts, it is hereby clarified that the rules made under this section shall not relate to imposition of fines or other pecuniary penalties or demand or payment of fees or contravention of any of the provisions of this Act or punishment therefor.

Sub-section (2) states that the Central Government may, by notification, frame a scheme to carry out the provisions of sub-section (1) through the electronic form.

Manner and Conditions of Filing: Rule 7 the Companies (Registration Offices and Fees) Rules, 2014 provides that every application, financial statement, prospectus, return, declaration, memorandum, articles, particulars of charges, or any other particulars or document or any notice, or any communication or intimation required to be filed or delivered or served under the Companies Act, 2013 and rules made thereunder, shall be filed or delivered or served:

- in computer readable electronic form, in portable document format (PDF); or

- in such other format as has been specified in any rule or form in respect of such application or form or document or declaration to the Registrar

through the portal maintained by the Central Government on its website or through any other website notified by the Central Government.

In case the documents are required to be filed on Non-Judicial Stamp Paper, the company shall submit such documents in the physical form, in addition to their submission in electronic form. Proof of delivery of documents submitted in physical form shall be scanned and form part of attachment to the e-form.

In case stamp duty on such documents is paid electronically through the portal maintained by the Central Government or through any other website notified by the Central Government, then, the company shall not be required to make physical submission of such documents, in addition to their submission in the electronic form.

Further it is provided that in respect of certain documents filed under the Act which are not covered for payment of stamp duty through the portal of the Central Government, and stamp duty payable on such documents in the respective State **is equal to or less than one hundred rupees**, the company shall scan such stamped documents complete in all respects and shall file electronically for evidencing by the Registrar and shall not be required to submit such documents, except those which are required to be filed for compounding of offences or adjudication of penalties or applications to Central Government or Regional Director in the physical form separately:

Unless otherwise stated in any law for the time being in force, the company shall retain such documents duly stamped in original permanently for the documents relating to incorporation and matters incidental thereto, changes in any of the clauses of the Memorandum and Articles of Association and in other cases for a minimum period of eight years from the date of filing of the documents and shall be required to produce the same as and when the same is required for inspection and verification by the competent authority under any law for the time being in force:

In addition, any correspondences (physically or electronically) and documents to be filed by any person shall contain name, designation, address, membership number or Director Identification Number, as the case may be, of the person signing such document and make sure correctness thereof and in no case, correspondence, merely with signature and writing authorised signatory shall be acceptable.

It is also provided that no request for recording any event based information or changes shall be accepted by the Registrar from such defaulting companies, unless they file their updated Balance Sheet and Profit and Loss Account and Annual Return with the Registrar of Companies except, -

- (i) filing of order of Court or other authorities,
- (ii) Balance Sheet and Profit and Loss Account,
- (iii) Compounding application,

- (iv) Form for transfer of money to Investor Education and Protection Fund,
- (v) Application for removal of the Auditor and
- (vi) GNL-1 for making company active.

Authentication of Documents: As regards authentication of documents Rule 8 of the Companies (Registration Office and Fees) Rules 2014 states as under:

- (1) An electronic form shall be authenticated by authorised signatories using digital signature.
- (2) Where there is any change in directors or secretaries, the form relating to appointment of such directors or secretaries has to be filed by a continuing director or the secretary of the company.
- (3) The authorised signatory and the professional, if any, who certify e-form shall be responsible for the correctness of the contents of e-form and correctness of the enclosures attached with the electronic form.
- (4) Every person authorised for authentication of e-forms, documents or applications etc., which are required to be filed or delivered under the Act or rules made there under, shall obtain a Digital Signature Certificate from the Certifying Authority for the purpose of such authentication and such certificate shall not be valid unless it is of class II or Class III specification under the Information Technology Act, 2000.
- (5) The electronic forms required to be filed under the Act or the rules thereunder shall be authenticated on behalf of the company by the Managing Director or Director or Secretary of the Company or other key managerial personnel.
- (6) Scanned image of documents shall be of original signed documents relevant to the e-forms or forms and the scanned document image shall not be left blank without bearing the actual signature of authorised person.
- (7) It shall be the sole responsibility of the person who is signing the form and professional who is certifying the form to ensure that all the required attachments relevant to the form have been attached completely and legibly as per provisions of the Act, and rules made thereunder to the forms or application or returns filed.
- (8) The documents or form or application filed may contain a power of attorney issued to an Advocate or Chartered Accountant or Cost Accountant or Company Secretary who is in whole time practice and to any others person supported by Board resolution to make representation to the registering or approving authority failing which a Director or key managerial personnel can make representation before such authority.
- (9) Where any instance of filing document, application or return etc, containing a false or misleading information or omission of material fact, requiring action under section 448 or section 449 is observed, the person shall be liable under section 448 and 449 of the Act.

- (10) Without prejudice to any other liability, in case of certification of any form, document, application or return under the Act containing wrong or false or misleading information or omission of material fact or attachments by the person, the Digital Signature Certificate shall be de-activated by the Central Government till a final decision is taken in this regard.
- (11) The Central Government shall set up and maintain for filing of electronic forms, documents and applications, and for viewing and inspection of documents in the electronic registry or for obtaining certified copies thereof-
- (a) a website or portal to provide access to the electronic registry; and
 - (b) as many Registrar's Facilitation Offices as may be necessary and at such places and for such time as the Central Government may determine.
- (12) (a) The following e-forms filed by companies, other than one person companies and small companies, under sub-rule (1) of rule 9, shall be pre-certified by the Chartered Accountant or the Company Secretary or as the case may be the Cost Accountant, in whole-time practice, namely:-
- INC-21, INC-22, INC-28, PAS-3, SH-7, CHG-1, CHG-4, CHG-9, MGT- 14, DIR-6, DIR-12, MR-1, MR-2, MSC-1, MSC-3, MSC-4, GNL-3, ADT-1, NDH-1, NDH-2, NDH-3;
- (b) The following e-forms filed by companies, other than one person companies and small companies, under sub-rule (1) of rule 9, shall be pre-certified in the following manner, namely:—
- (i) GNL-1 – optional pre-certification by the Chartered Accountant or the Company Secretary or as the case may be the Cost Accountant, in whole-time practice;
 - (ii) DPT-3 – certification by Auditors of the company;
 - (iii) MGT-10-certification by a Company Secretary in whole-time practice
 - (iv) “AOC-4 certification by the Chartered Accountant or the Company Secretary or as the case may be the Cost Accountant, in whole-time practise.”
- (c) E-form DIR-3 shall be filed along with attestation of photograph, identity proof and proof of residence of the applicant by the Chartered Accountant or the Company Secretary or as the case may be the Cost Accountant, in whole-time practice.

e-Forms

Prior to the e-Governance programme through MCA21 on-line Portal, all transactions including statutory filings by companies, were conducted in manual mode using the prescribed physical paper forms. In order to make physical forms compatible with the e-Governance processes, they have been re-engineered and converted into electronic forms (e-Forms).

The e-Forms have been designed with the in-built “pre-fill” feature. This feature enables the data in the required fields being captured from the database available in the electronic registry in an automated manner. Accordingly, requirements of repetitive data entry have been significantly reduced.

The process of electronic filing also incorporates the facility of “pre-scrutiny” of the e-Form. This is a completely electronic process where the system verifies if the form is complete in all respect. This is, however, limited to such checks as can be performed by the computerized system.

Electronic address

The companies may interact through the on-line Portal as provided by MCA. Alternatively, they use valid e-mail IDs of their own or of authorised representatives to enable the offices of the Central Government to inter-act with them.

Director Identification Number (DIN)

As part of the e-governance programme, the concept of Director Identification Number (DIN) has been introduced. The DIN is in the form of a unique identifier for an existing or a future intending director, containing personal information about such director. This would not only help in fixing the identity of the person but also co-relate his participation in other companies, either past or present.

System Requirements For E-Filing

- (a) Windows 2000 or later version as Operating System.
- (b) Internet connection to access the MCA website.
- (b) Internet Explorer Version 10 or above, Google Chrome 49 or above, Mozilla Firefox 45 or above.
- (c) Adobe Reader from version 11 or later
- (d) Java Runtime Environment (JRE – Java version 8 Update 92 is suggested).
- (e) Scanner for scanning documents to be used as attachments.
- (f) Printer for printing bank challan or service fee payment receipt, etc.
- (g) Enabling of Pop-ups from MCA21 Portal in the browser.

Process Involved in e-Filing

The process involved in e-Filing of various documents is stated as under:

1. Registration Requirements

- (i) Due to the fact that only registered users will be allowed to do e-filing, the user must get himself registered at the on-line Portal of MCA21. Registration is a one-time process through which the user creates his personalised login ID. This ensures security and also serves as a channel for providing personalized information as the functionality evolves.

- (ii) In case the user has got a Digital Signature Certificate (DSC) and if he intends to sign the e-forms as an authorized signatory, he will need to register his DSC also.
- (iii) The process of registration of DSC will be repeated every time when the user procures a new DSC or renew his DSC.

2. Downloading of e-Form

- (i) e-Forms are freely downloadable and are in the 'PDF' format. The user is required to use new set of notified e-Forms that are being made available in the MCA21 portal.
- (ii) Instruction kit for each e-Form is also available alongside the e-Forms.
- (iii) It is not necessary to download the e-Form each time, but it is to ensured that the user has the latest e-Forms.

3. Completion of e-Form

- (i) e-Forms are specifically tailored by MCA to meet the e-filing needs. The user may fill-in an e-Form either on-line or off-line.
- (ii) On-line e-Form filling requires active internet connection whereas off-line form filling can be done without staying connected.
- (iii) The e-Forms can be filled-in and signed digitally using an Acrobat Reader.
- (iv) Certain fields of e-forms can be filled-up automatically by the System (to the extent such data is available in the database of MCA) by selecting the "pre-fill" option.
- (v) The user can do "automated pre-scrutiny" of e-form. Use of this facility ensures that the e-Form is complete in all respects and is good for e-filing.
- (vi) The user may also attach supporting documents, if applicable. However, it must be ensured that the supporting documents are in PDF format. Wherever possible, the size of the attachments must be kept at minimal.

Note: As an additional facility, support for conversion of popular formats such as Microsoft Office into PDF is being made available in the MCA21 portal itself.

- (vii) After completion, the user is required to sign the e-form using the Digital Signature Certificate (DSC).
- (viii) If there are more than one signatories, the user can send the e-form either on suitable media or as an email attachment (or transfer a file over the network) to other individuals for signing the requisite e-form digitally.

Note: Multiple signatures can be applied on a given e-Form, but it must be ensured that contents of the e-form are not altered after it has been signed. In case the contents are altered at any stage, the document will become invalid and will be rejected during the e-filing process.

- (ix) After all individuals have digitally signed the form, it is ready for submission.

4. Submission of e-Form

- (i) In case the user wants to carry out e-filing, he will need to be connected to the Internet.
- (ii) Submission of e-form will need to be made at the MCA21 portal using specialized functionality that is provided at the portal.

Note: Sending the e-Form by email does not constitute e-filing and therefore, it needs to be avoided.

- (iii) Submission of e-Form will generally take a few minutes. However, it will depend on the size of e-form/attachments and the speed/quality of the Internet connection.
- (iv) If the e-form is defective as may be identified by the MCA21 system during submission, it will be rejected and returned to the user with clear details of the nature of the defect.

Note: The defect may crop in as a result of incorrect data that might have been entered in the e-Form or it may be due to missing or invalid digital signatures.

- (v) If the e-Form is correct in all respects, the user can proceed to the next step of making payment.

Note: The copy of the document that has been submitted remains in the possession of the user and he may retain this as a part of his records.

5. Making of Payment

- (i) In accordance with the applicable law, fee calculation will be done automatically by the system. The fee for the service will be displayed to the user.
- (ii) The user will be asked to choose any one of the following methods of payment:
 - Credit Card/Debit Card
 - Internet Banking
 - NEFT
 - Physical Challan (i.e. at Bank counter)
 - Pay Later
- (iii) In the case of payment mode of Credit Card/Debit Card, Internet Banking, etc. the computer of the authorized bank will take over at this stage to carry forward the transaction to completion. System will generate a receipt that the user can retain as a part of his records.
- (iv) In the case of challan payment, a fully completed challan will be generated by the system that can be printed by the user and taken to any of the nearest authorized branch. He may choose to pay either through cash (limits as stipulated by Law will be applicable) or through a local cheque or DD. The acknowledged copy of the challan will serve as the receipt.

- (v) Once the user has made the payment in the Bank following the challan payment system, the filing shall be complete. Based on confirmation of payment by the bank to the MCA21 system, the document will be transmitted to the Back Office for further processing.
- (vi) In case of Pay Later, e-form can be uploaded on MCA portal in one step and make the payment at later point of time using the online payment mode i.e., Credit Card/Debit Card, Internet Banking, etc. An e-challan generated at the time of uploading e-form contains the validity date within which payment shall be made by the user.

6. Completion of e-Filing

e-Filing will be completed once the necessary payment is remitted either through electronic payment means or through the challan-based method. Banks will authorize the transactions after which the documents filed by the user will be electronically forwarded to the concerned RoC office (also referred to as Back Office) for further processing. The user will also be provided a facility at MCA21 portal to check if the e-filing has been completed successfully. The challan number or Service Request Number (SRN) that is printed on the challan or the computer-generated receipt will be helpful for future referencing of his service request.

Extensible Business Reporting Language (XBRL)

XBRL is an open, royalty-free software specification developed by XBRL International (XII), a global not-for-profit organisation founded by American Institute of Certified Public Accountants (AICPA), with an aim to improve the accountability and transparency of business performance globally by providing the open data exchange standard for business reporting.

Being an international standards organization, XBRL International (XII) develops and maintains the XBRL standards and related specifications in order to improve business reporting for the public good.

India is now an established jurisdiction of XBRL International. A separate company, under section 25 has been created, to manage the operations of XBRL India. The main objectives of XBRL India are:

- To create awareness about XBRL in India
- To develop and maintain Indian Taxonomies
- To help companies, adopt and implement XBRL.

Meaning:

According to Rule 2 (1) (d) of the Companies (Filing of Documents and Forms in Extensible Business Reporting Language) Rules, 2015, 'Extensible Business Reporting Language (XBRL)' means a standardised language for communication in electronic form to express, report or file financial information by the companies under the Companies Act, 2013.

Thus, it is a language for the electronic communication of business and financial data. Its extensible nature means that it can be adjusted to meet particular business requirements, even at the individual organization level. Since XBRL is extensible and flexible, it can be adapted to a wide variety of different requirements.

Benefits:

- XBRL language is economical, faster, more reliable and more accurate in handling data. Its use results in improved analysis and in providing better quality of information and decision-making.
- XBRL enables producers and consumers of financial data to switch resources away from costly manual processes, typically involving time-consuming comparison, assembly and re-entry of data.
- Being a flexible language, it supports all current aspects of reporting in different countries and industries.
- Comparability is easier, as it helps in identifying data which is genuinely alike. Also, it helps in distinguishing information which is not comparable.
- XBRL increases the usability of financial statement information. The need to re-key financial data for analytical and other purposes can be eliminated.
- With full adoption of XBRL, companies can automate data collection, e.g. data from different divisions of a company with different accounting systems can be assembled quickly, cheaply and efficiently.

Working:

XBRL makes the data readable, with the help of following two documents:

- Taxonomy
- Instance Document

According to Rule 2 (1) (e) of the Companies (Filing of Documents and Forms in Extensible Business Reporting Language) Rules, 2015, 'Taxonomy' means in XBRL, an electronic dictionary for reporting the business data as approved by the Central Government in respect of any documents or forms indicated in these rules.

Based on the regulatory requirements, taxonomy defines various elements and also their relationships. Using the prescribed taxonomy, companies are required to map their reports and generate a valid XBRL Instance Document.

The process of mapping indicates matching the concepts as reported by the company to the corresponding element in the taxonomy. In addition to assigning XBRL tag from taxonomy, information like unit of measurement, period of data, scale of reporting etc., needs to be included in the Instance Document.

XBRL (eXtensible Business Reporting Language) as it defines the specific elements, concepts, and relationships that can be used for reporting financial and non-financial data. Here's an example of a taxonomy in relation to XBRL:

Let's consider a fictional company called XYZ Corp. that needs to report its financial statements using XBRL. The taxonomy for XYZ Corp. might include the following elements:

Company Name: This element represents the name of the company, such as "XYZ Corp."

Balance Sheet: This element represents the financial statement category. It includes sub-elements like "Assets," "Liabilities," and "Equity."

Current Assets: This element represents a subset of assets that can be easily converted into cash within one year. It includes sub-elements like "Cash and Cash Equivalents," "Accounts Receivable," and "Inventory."

Long-term Debt: This element represents a type of liability that will be paid off over a period longer than one year.

Net Income: This element represents the company's total revenue minus expenses over a given period.

Earnings per Share (EPS): This element represents the company's net income divided by the average number of outstanding shares.

Statement of Cash Flows: This element represents another financial statement category, which includes sub-elements like "Operating Activities," "Investing Activities," and "Financing Activities."

These are just a few examples of elements that would be part of XYZ Corp.'s XBRL taxonomy. The taxonomy would define the hierarchical structure of these elements, their data types, and any applicable calculations or relationships between them. This allows companies and regulatory bodies to standardize and exchange financial information in a machine-readable format using XBRL.

Taxonomies for Indian companies are developed based on the requirements of:

- Schedule III of Companies Act, 2013;
- Accounting Standards, issued by ICAI; and
- SEBI Listing requirements.

There are more than 5500 taxonomies based on Company Law requirements, IND AS / I GAAP requirements, MCA reporting requirements, Schedule III, MSME reporting's, and SEBI reporting's.

Following is the content relating to related parties taxonomy covering various provisions of Company Law, IND AS, Schedule III etc.,

Prefix	Label	Publisher	Reference	Reference para
in-ca	Amount paid as advances if any for contracts/arrangements/transactions with related party	MCA	Form AOC-2	Form AOC-2
in-ca	Amount paid as advances if any for material contracts/arrangements/transactions with related party	MCA	Form AOC-2	Form AOC-2
in-ca	CIN of related party	MCA		
in-ca	Country of incorporation or residence of related party	MCA		
in-ca	Dates of approval of contracts/arrangements/transactions with related party by board	MCA	Form AOC-2	Form AOC-2
in-ca	Dates of approval of material contracts/arrangements/transactions with related party by board	MCA	Form AOC-2	Form AOC-2
in-ca	Dates on which special resolution passed in general meeting for contracts/arrangements/transactions with related party required by section 188 of companies act, 2013	MCA	Form AOC-2	Form AOC-2
in-ca	Description of nature of contracts/arrangements/transactions with related party	MCA	Form AOC-2	Form AOC-2
in-ca	Description of nature of material contracts/arrangements/transactions with related party	MCA	Form AOC-2	Form AOC-2
in-ca	Disclosure in auditors report relating to transactions with related parties	MCA	Companies Auditors Report Order, 2020	
in-ca	Duration of contracts/arrangements/transactions with related party	MCA	Form AOC-2	Form AOC-2
in-ca	Duration of material contracts/arrangements/transactions with related party	MCA	Form AOC-2	Form AOC-2

in-ca	Identification number of foreign related party in country of incorporation or residence	MCA		
in-ca	Nature of related party relationship	MCA	Form AOC-2	Form AOC-2
in-ca	Particulars of contracts/arrangements with related parties under section 188(1) [Text Block]	MCA	Companies Act, 2013	Section 134(3)
in-ca	Permanent account number of related party	MCA		
in-ca	Gross value of transaction with related parties	MCA	Form AOC-4	
in-ca	Bad debts of related parties	MCA	Form AOC-4	
in-ca	Gross value of transactions with related parties	MCA	Form AOC-4	Form AOC-4
ind-as	Advances given other related parties [Member]	MCA	Schedule III	General Instructions - Balance sheet -A. X (ii) (1)(b) -MCA Requirement
ind-as	Advances given other related parties [Member]	MCA	Schedule III	General Instructions - Balance sheet -B. VI (i) (1) (b) - MCA Requirement
ind-as	Advances to related parties [Member]	MCA	Schedule III	General Instructions - Balance sheet -A. X (ii) (1)(b)
ind-as	Advances to related parties [Member]	MCA	Schedule III	General Instructions - Balance sheet -B. VI (i) (1) (b)
ind-as	Amounts payable related party transactions	ICAI	Indian accounting standard	Ind AS 24 18 b
ind-as	Amounts payable related party transactions	ICAI	Indian accounting standard	Ind AS 24 20

ind-as	Amounts receivable related party transactions	ICAI	Indian accounting standard	Ind AS 24 20
ind-as	Amounts receivable related party transactions	ICAI	Indian accounting standard	Ind AS 24 18 b
ind-as	Commitments made by entity, related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 i
ind-as	Commitments made on behalf of entity, related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 i
ind-as	Description of accounting policy for transactions with related parties [Text Block]	ICAI	Indian accounting standard	Ind AS 1 117 b
ind-as	Description of nature of transactions with related party	ICAI	Indian accounting standard	Ind AS 24 18
ind-as	Details of advance to related parties	MCA	Schedule III	General Instructions - Balance sheet -A. X - Common practice
ind-as	Details of advance to related parties	MCA	Schedule III	General Instructions - Balance sheet -B. VI - Common practice
ind-as	Details of loans to related parties	MCA	Schedule III	General Instructions - Balance sheet -A. VIII. (i) (b)
ind-as	Details of loans to related parties	MCA	Schedule III	General Instructions - Balance sheet -B. V. (i) (b)
ind-as	Disclosure of related party [Text Block]	ICAI	Indian accounting standard	Ind AS 24 Disclosures

ind-as	Disclosure of transactions between related parties [Text Block]	ICAI	Indian accounting standard	Ind AS 24 18
ind-as	Disclosure of transactions between related parties [Table]	ICAI	Indian accounting standard	Ind AS 24 19
ind-as	Other related parties [Member]	ICAI	Indian accounting standard	Ind AS 24 19 (g)
ind-as	Disclosure that related party transactions were made on terms equivalent to those that prevail in arm's length transactions	ICAI	Indian accounting standard	Ind AS 24 23
ind-as	Expense recognised during period for bad and doubtful debts for related party transaction	ICAI	Indian accounting standard	Ind AS 24 18 d
ind-as	Explanation of details of guarantees given or received of outstanding balances for related party transaction	ICAI	Indian accounting standard	Ind AS 24 18 b ii
ind-as	Explanation of terms and conditions of outstanding balances for related party transaction	ICAI	Indian accounting standard	Ind AS 24 18 b i
ind-as	Guarantee given for related parties [Member]	ICAI	Common practice	
ind-as	Leases as lessee related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 d
ind-as	Leases as lessor related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 d
ind-as	Loans and advances from related parties [Member]	MCA	Schedule III	General Instructions - Balance sheet -E (I)(ii) (e)
ind-as	Loans and advances from related parties [Member]	MCA	Schedule III	General Instructions - Balance sheet -F(I)(i)(b)

ind-as	Loans given other related parties [Member]	MCA	Schedule III	General Instructions - Balance sheet -A. VIII(i)(b) - MCA Requirement
ind-as	Loans given other related parties [Member]	MCA	Schedule III	General Instructions - Balance sheet -B. V. (i)(b) - MCA Requirement
ind-as	Loans to related parties [Member]	MCA	Schedule III	General Instructions - Balance sheet -A. VIII(i)(b)
ind-as	Loans to related parties [Member]	MCA	Schedule III	General Instructions - Balance sheet -B. V. (i)(b)
ind-as	Name of related party	ICAI	Indian accounting standard	Ind AS 24; common practice
ind-as	Outstanding commitments made by entity, related party transactions	ICAI	Indian accounting standard	Ind AS 24 18 b
ind-as	Outstanding commitments made on behalf of entity, related party transactions	ICAI	Indian accounting standard	Ind AS 24 18 b
ind-as	Participation in defined benefit plan that shares risks between group entities, related party transactions	ICAI	Indian accounting standard	Ind AS 24 22
ind-as	Provision of guarantees or collateral by entity related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 h
ind-as	Provision of guarantees or collateral to entity related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 h

ind-as	Provisions for doubtful debts related to outstanding balances of related party transaction	ICAI	Indian accounting standard	Ind AS 24 18 c
ind-as	Purchases of goods related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 a
ind-as	Purchases of property and other assets, related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 b
ind-as	Revenue from rendering of services related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 c
ind-as	Revenue from sale of goods related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 a
ind-as	Sales of property and other assets, related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 b
ind-as	Services received related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 c
ind-as	Settlement of liabilities by entity on behalf of related party, related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 j
ind-as	Settlement of liabilities on behalf of entity by related party, related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 j
ind-as	Statement that rate regulator is related party	ICAI	Indian accounting standard	Ind AS 114 30 b
ind-as	Transfers of research and development from entity related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 e
ind-as	Transfers of research and development to entity related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 e

ind-as	Transfers under finance agreements from entity, related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 g
ind-as	Transfers under finance agreements to entity, related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 g
ind-as	Transfers under license agreements from entity related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 f
ind-as	Transfers under license agreements to entity related party transactions	ICAI	Indian accounting standard	Ind AS 24 21 f
ind-as	Whether there are any related party transactions during year	ICAI	Common practice	
ind-as	Description of nature of related party relationship	ICAI	Indian accounting standard	Ind AS 24; common practice
ind-as	Other related party transactions expense	ICAI	Indian accounting standard	Ind AS 24 21
ind-as	Other related party transactions income	ICAI	Indian accounting standard	Ind AS 24 21
ind-as	Other related party transactions contribution made	ICAI	Indian accounting standard	Ind AS 24 21
ind-as	Other related party transactions contribution received	ICAI	Indian accounting standard	Ind AS 24 21
in-ca	Whether Approval Taken From Board For Material Contracts Arrangements Transactions With Related Party	MCA	Specific requirement	

Creation of Financial Statements:

There are a number of ways to create financial statements in XBRL. Accordingly:

- XBRL-aware accounting software products which support the export of data in XBRL form, allow the users to map charts of accounts and other structures to XBRL tags.
- By using XBRL software tools, statements can be mapped into XBRL.
- Data from accounting databases can be extracted into XBRL format.
- Applications can transform data in particular formats into XBRL. The route which an individual company may take will depend on its requirements and the accounting software and systems used by it, among other factors.

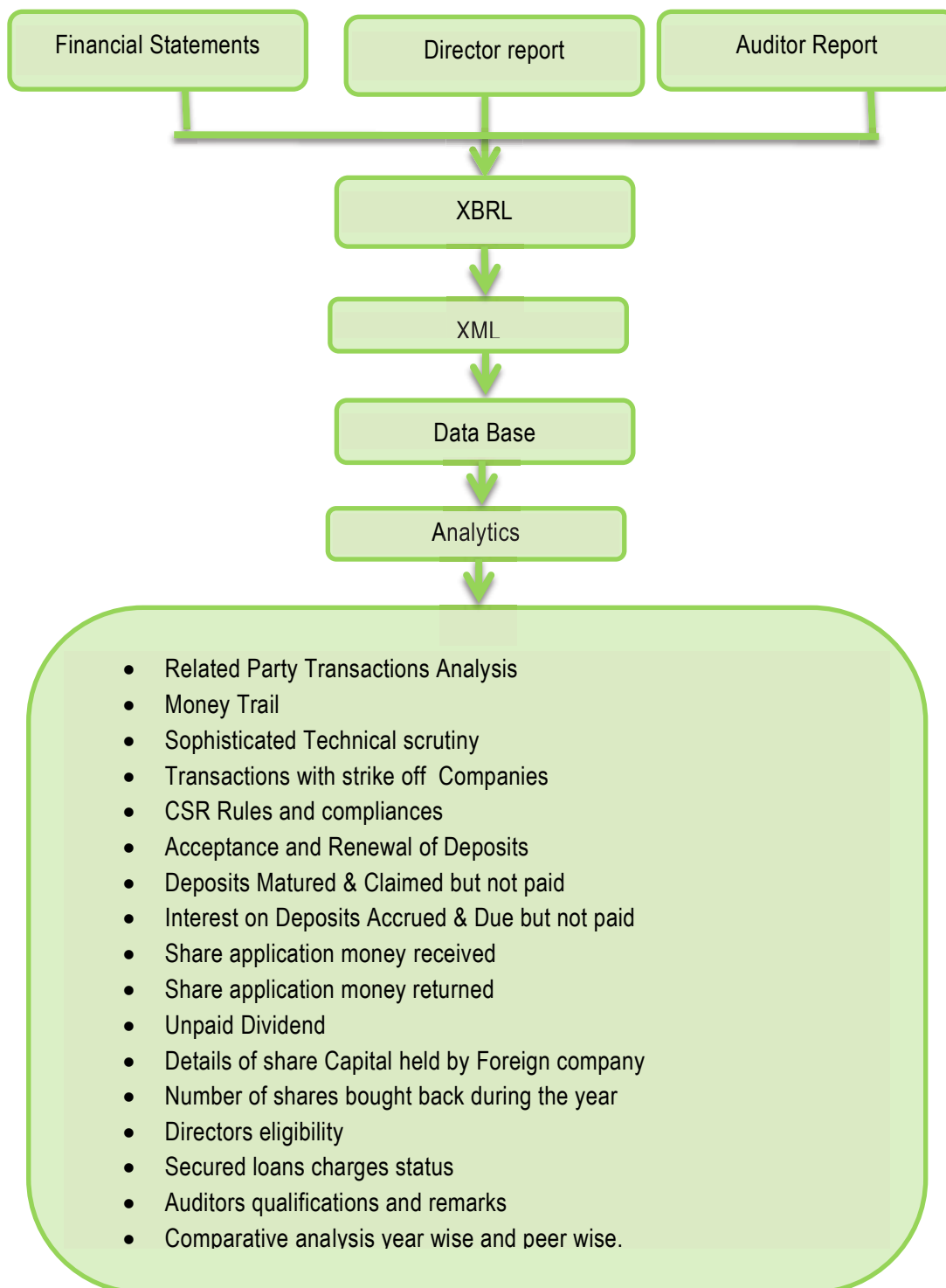
Statutory Requirements:

According to Rule 3 (1) of the Companies (Filing of Documents and Forms in Extensible Business Reporting Language) Rules, 2015, the following class of companies shall file their financial statements and other documents under section 137 of the Companies Act, 2013 with the Registrar in e-Form AOC-4 XBRL as per Annexure-I:

- (i) Companies listed with stock exchanges in India and their Indian subsidiaries;
- (ii) Companies having paid-up capital of five crore rupees or above;
- (iii) Companies having turnover of one hundred crore rupees or above;
- (iv) All companies which are required to prepare their financial statements in accordance with Companies (Indian Accounting Standards) Rules, 2015.

Provided that the companies preparing their financial statements under the Companies (Accounting Standards) Rules, 2006 shall file the statements using the Taxonomy provided in Annexure-II and companies preparing their financial statements under Companies (Indian Accounting Standards) Rules, 2015, shall file the statements using the Taxonomy provided in Annexure-II A.

The Company which has once filed its financial statements in XBRL format, shall continue to file its financial statements and other documents in XBRL format though it may not fall under the class of companies as mentioned above in succeeding years.



Case study

X Company, being a listed company, can follow the below process to validate and confirm related party transactions using the public domain:

To leverage technology, X Company can adopt the following steps:

As a listed company, X Company is required to file XBRL (eXtensible Business Reporting Language) reports. These reports contain specific codes, including 4-digit and 8-digit codes, that identify various disclosures and requirements in compliance with the Companies Act, 2013.

The XBRL taxonomy associated with the codes pertains to the Sales and Particulars of Cost of Goods sold.

X Company can access the XML files of similar companies available on the MCA (Ministry of Corporate Affairs) portal. These XML files contain valuable data related to similar products.

By utilizing XML data analysis techniques, X Company can extract and analyze data from the XML files of similar companies. This analysis can provide insights into the average profitability of similar products.

Armed with the information obtained from the XML data analysis, X Company can establish arm's length pricing for related party transactions. This approach helps prevent fraudulent practices and ensures fair and transparent dealings.

By employing XML data analysis techniques and leveraging public domain data available through XBRL filings, X Company can effectively validate related party transactions and mitigate the risk of fraudulent activities.

Example: From the database of companies XBRL XML, comparatives of companies manufacturing batteries can be generated.

Sectoral Screener

Net Profit

Criteria

Market Capitalisation

Net Sales

Net Profit

Total Assets

Other Income

Interest

Tax

EPS

Sundry Debtors

Cash/Bank

Inventory

Debt

Contingent Liabilities

Batteries

GO

Batteries

	Last Price	Change	% Change	Net Profit (Rs. cr)
	237.35	5.40	2.33	903.63
	678.55	23.45	3.58	694.41
	151.50	-1.70	-1.11	95.54
High Energy	520.00	5.35	1.04	20.50
Eveready Ind	341.25	-2.70	-0.79	20.13
Indo-National	402.00	6.05	1.53	1.00
Standard Batter	28.79	-0.01	-0.03	-5.37
Panasonic Energy	260.00	6.95	2.75	-10.64

Exemptions

According to second Proviso to Rule 3 (1) non-banking financial companies, Housing Finance Companies and Companies engaged in the business of Banking and Insurance sector are exempted from filing of financial statements under these rules.

List of Important e-Forms

Description	e-Form
Information to the Registrar by company regarding the number of layers of subsidiaries.	Form CRL-1
Particulars of person(s) or Key managerial personnel(s) charged or specified for the purpose of sub-clause (iii) or (iv) of clause (60) of section 2	Form GNL-3

Approval Services (Headquarters)

Description	e-Form
Form of intimation of appointment of cost auditor by the company to Central Government.	Form CRA-2
Form for filing application or documents with Central Government	Form CG-1

Approval Services (Regional Director)

Description	e-Form
Application for removal of auditor(s) from his/their office before expiry of term	Form ADT-2
Memorandum of Appeal to be filed against the order of the adjudicating officer with the Regional Director	Form ADJ
Form for filing Addendum for Rectification of Defects or Incompleteness	Form RD GNL-5
Applications made to Regional Director	Form RD-1
Application to RD for conversion of section 8 company into company of any other kind	Form INC-18
Application to RD for approval to shift the Registered Office from one state to another state or from jurisdiction of one Registrar to another Registrar within the same state	Form INC-23
Application to Central Government for extension of time for filing particulars of registration of satisfaction of charge OR for rectification of omission or mis-statement of any particular in respect of creation/ modification/ satisfaction of charge	Form CHG-8
Application for extension of time	NDH-2
Application for approval of Central Government for change of name	INC-24

Approval Services (Registrar of Companies)

Description	e-Form
Application by company to ROC for removing its name from register of Companies	Form STK-2
Applications made to Registrar of Companies	Form GNL-1
Application for striking off the name of company under the Fast Track Exit (FTE) Mode	Form FTE
Application to RoC for obtaining the status of Dormant Company	Form MSC-1
Application to RoC for obtaining the status of Active Company	Form MSC-4
Application for grant of license to an existing company under section 8	Form INC-12
One Person Company- Application for conversion	Form INC-6

Change Services

Description	e-Form
One Person Company- Nominee consent form	Form INC-3
One Person Company- Change in member/nominee	Form INC-4
Notice of situation or change of situation of registered office to be filed with registrar of companies	Form INC-22
Conversion of public company into private company or private company into public company and conversion of unlimited liability company into a company limited by shares or guarantee	Form INC-27
Notice to the Registrar of any alteration of share capital	Form SH-7
Return of alteration in the documents filed for registration by Foreign Company to be filed with the registrar of companies	Form FC-2
Annual Accounts along with the list of all principal places of business in India established by Foreign Company	Form FC-3

DIN related Forms

Description	e-Form
Application for allotment of Director Identification Number before appointment in an existing company	Form DIR-3
Application for cancellation or surrender or deactivation of Director Identification Number	Form DIR-5
Intimation of change in particulars of Director to be given to the Central Government	Form DIR-6
A Report by a company to ROC for intimating the disqualification of the director under sub-section (2) of Section 164 of the Act.	Form DIR-9

Application for KYC of Directors	Form DIR-3 KYC/DIR-3 KYC WEB
Notice of resignation of a director to the Registrar	Form DIR-11
Intimation of Director Identification number by the company to the registrar	Form DIR-3C
Particulars of appointment of directors and the key managerial personnel and the changes among them , resignation/ consent of director to be filed with the Registrar of Companies	Form DIR-12
Application for removal of disqualification of directors	Form DIR-10

Charge Related Forms

Description	e-Form
Application for registration of creation, modification of charge (other than those related to debentures) including particulars of modification of charge by Asset Reconstruction Company in terms of securitization and reconstruction of Financial Assets and Enforcement of Securities Interest Act, 2002 (SARFASI)	Form CHG-1
Particulars for satisfaction of charge thereof	Form CHG-4
Notice of appointment or cessation of receiver or manager to be filed with Registrar of Companies	Form CHG-6
Application for registration of creation or modification of charge for debentures or rectification of particulars filed in respect of creation or modification of charge for debentures	Form CHG-9

Incorporation services

Description	e-Form
Registration of Entities for undertaking CSR Activities	Form CSR-1
Active Company Tagging Identities and Verification (ACTIVE)	Form INC-22A
One Person Company- Nominee consent form	Form INC-3
Simplified Proforma for Incorporating Company Electronically - with mandatory PAN and TAN application included	Form SPICe+
eMemorandum of Association	Form INC 33 - SPICe MOA
eArticles of Association	Form INC 34 - SPICe AOA
Application by a company for registration u/s 366	Form URC-1
Information to be filed by foreign company with the Registrar of Companies	Form FC-1
Application for Goods and Services Tax Identification number, Employees State Insurance Corporation registration plus Employees Provident Fund	Form AGILE-PRO-S

Organization registration, Profession tax Registration (in Maharashtra) and opening of bank account and Shops and Establishment Registration	
Application for change of name of existing company	FORM RUN

Compliance Related Filing

Description	e-Form
Return to the Registrar in respect of declaration under section 90	Form BEN-2
Form for furnishing half yearly return with the registrar in respect of outstanding payments to Micro or Small Enterprise.	Form MSME I
Form for filing Cost Audit Report with the Central Government.	Form CRA-4
Information to the Registrar by Company for appointment of Auditor	Form ADT-1
Notice of Resignation by the Auditor	Form ADT-3
Return to the Registrar in respect of declaration under section 89	Form MGT-6
Return of Deposits	Form DPT-3
Return of Allotment of securities	Form PAS-3
Letter of Offer to be filed with the Registrar of Companies in case of buy-back	Form SH-8
Declaration of Solvency to be filed with Registrar of Companies in case of Buy back	Form SH-9
Return in respect of buy-back of securities	Form SH-11
Form for submission of documents with the Registrar of Companies	Form GNL-2
Filing of Resolutions and Agreements to the ROC	Form MGT-14
Annual Return of a Foreign Company to be filed with Registrar of Companies	Form FC-4
Return of Dormant Companies to be filed with Registrar of Companies	Form MSC-3
Return of statutory compliances	Form NDH-1
Return of Nidhi company for the half-year ended	Form NDH-3
Application for declaration as Nidhi company and for up-dation of status by Nidhi	Form NDH-4
Reconciliation of Share Capital Audit Report (Half-yearly)	Form PAS-6

Provisions related to Managerial Personnel

Description	e-Form
Form of application to the Central Government for approval of the appointment	Form MR-2

or reappointment and remuneration or increase in remuneration or waiver for excess or over-payment to managing director/whole time director/manager and commission or remuneration to director without complying the with Part I of Schedule V of Companies Act 2013	
Return of appointment of MD/WTd/manager	Form MR-1

Informational Services

Description	e-Form
Notice of situation or change of situation or discontinuance of situation, of place where foreign register shall be kept to be filed with the Registrar of Companies	Form MGT-3
Form for filing Report on Annual General Meeting	Form MGT-15
Reply to Call for Information on CSR	Form CFI (CSR)
Intimation to Registrar of Companies of revocation/surrender of license issued under section 8	Form INC-20
Declaration for commencement of business	Form INC-20A
Notice of Order of the Court or any other competent authority	Form INC-28
Notice of address at which books of accounts are maintained	Form AOC-5
Report by Statutory Auditors to Central Government related to Fraud.	Form ADT-4
Form for filing addendum for rectification of defects or incompleteness.	Form GNL-4

Investor Services

Description	e-Form
Investor Complaint Form	Form ICP
Serious Complaint Form	Form SCP

Annual filing

Description	e-Form
Form for filing financial statement and other documents with the Registrar for NBFCs	Form AOC-4 NBFC (Ind AS)
Form for filing consolidated financial statements and other documents with the Registrar for NBFCs	Form AOC-4 CFS NBFC (Ind AS)
Form for filing financial statement and other documents with the Registrar	Form AOC-4
Form for filing consolidated financial statements and other documents with the Registrar	Form AOC-4 (CFS)

Form for filing XBRL document in respect of financial statement and other documents with the Registrar	Form AOC-4 (XBRL)
Form for filing annual return by a company.(other than OPC's and Small Companies)	Form MGT-7
Form for filing abridged annual return by OPCs and Small company.	Form MGT-7A
Report on CSR	Form CSR-2

Refund Form

Description	e-Form
Application for requesting refund of fees paid	Form Refund

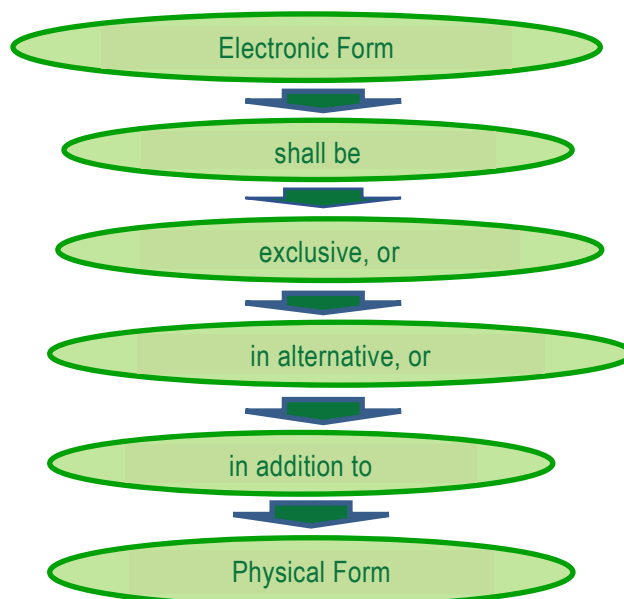
Attachments

Description	Attachment with Help Kit
Circular or circular in the form of advertisement inviting deposits	Form DPT-1
Private Placement Offer Cum Application letter	Form PAS-4



3. ELECTRONIC FORM TO BE EXCLUSIVE, ALTERNATIVE OR IN ADDITION TO PHYSICAL FORM [SECTION 400]

The Central Government may also provide in the rules made under section 398 and section 399 that the electronic form for the purposes specified in these sections shall be exclusive, or in the alternative or in addition to the physical form, therefor.





4. PROVISION OF VALUE-ADDED SERVICES THROUGH ELECTRONIC FORM [SECTION 401]

The Central Government may provide such value-added services through the electronic form and levy such fee thereon as may be prescribed.



5. APPLICATION OF PROVISIONS OF INFORMATION TECHNOLOGY ACT, 2000 [SECTION 402]

All the provisions of the Information Technology Act, 2000 relating to the electronic records, including the manner and format in which the electronic records shall be filed, in so far as they are not inconsistent with this Act, shall apply in relation to the records in electronic form specified under section 398.



6. FEE FOR FILING ETC. [SECTION 403]

Section 403 of the Companies Act, 2023 deals with fee for filing, etc. According to Section 403 (1), any document, required to be submitted, filed, registered or recorded, or any fact or information required or authorised to be registered under this Act, **shall be submitted, filed, registered or recorded within the time specified in the relevant provision on payment of such fee as may be prescribed.**

Provided that where any document, fact or information required to be submitted, filed, registered or recorded, as the case may be, under section 92 or 137 is not submitted, filed, registered or recorded, as the case may be, within the period provided in those sections, without prejudice to any other legal action or liability under this Act, it may be submitted, filed, registered or recorded, as the case may be, after expiry of the period so provided in those sections, on payment of such additional fee as may be prescribed, which shall not be less than one hundred rupees per day and different amounts may be prescribed for different classes of companies.

Provided further that where the document, fact or information, as the case may be, **in cases other than referred to in the first proviso, is not submitted, filed, registered or recorded,** as the case may be, within the period provided in the relevant section, it may, without prejudice to any other legal action or liability under this Act, be submitted, filed, registered or recorded as the case may be, on payment of such additional fee as may be prescribed and different fees may be prescribed for different classes of companies.

Provided also that where there is **default on two or more occasions in submitting, filing, registering or recording of such document, fact or information,** as may be prescribed, it may, without prejudice to any other legal action or liability under this Act, be submitted, filed, registered or recorded, as the case may be, on payment of such higher additional fee, as may be prescribed.

According to Section 403 (2), where a **company fails or commits any default to submit, file, register or record any document, fact or information under sub-section (1) before the expiry of the period specified in the relevant section**, the company and the officers of the company who are in default, shall, without prejudice to the liability for the payment of fee and additional fee, be liable for the penalty or punishment provided under this Act for such failure or default.

As regards fees, **Rule 12 of the Companies (Registration Offices and Fees) Rules, 2014** states as under:

Rule 12 (1): The documents required to be submitted, filed, registered or recorded or any fact or information required or authorised to be registered under the Act shall be submitted, filed, registered or recorded on payment of the fee or on payment of such additional fee as applicable, as mentioned in Table *annexed to these rules (refer Annexure given below).

Rule 12 (2): For the purpose of filing the documents or applications for which no e-form is prescribed under the various rules prescribed under the Act, the document or application shall be filed through Form No. GNL.1 or GNL.2 along with fee as applicable and in case a single form is prescribed for multiple purposes, the fee shall be paid for each of the purposes contained in the single form.

Rule 12 (3): For the purpose of filing information to sub-clause (60) of Section 2 of the Act, such information shall be filed in Form No. GNL.3 along with fee as applicable.

Rule 13 of the Companies (Registration Offices and Fees) Rules, 2014 describes the mode of payment of fees and states that the fees, charges or other sums payable for filing any application, form, return or any other document in pursuance of the Act or any rule made thereunder shall be paid by means of credit card; or internet banking; or remittance at the counter of the authorised banks or any other mode as approved by the Central Government.

ANNEXURE**TABLE OF FEES***[Pursuant to Rule 12 of the Companies (Registration Offices and Fees) Rules, 2014]***I. FEE FOR FILINGS ETC. UNDER SECTION 403 OF THE COMPANIES ACT, 2013**

Table of fees for the documents required to be submitted, filed, registered or recorded or for any fact or information required or authorized to be registered under the Act, shall be submitted filed, registered or recorded within the time specified in the relevant provision on payment of fee as prescribed hereunder:

A. Table of Fees to be Paid to the Registrar

(I) In respect of a company having a share capital:	Other than OPCs and Small Companies (in rupees)	OPC and Small Companies (in rupees)
1. (a) For registration of OPC and small companies whose nominal share capital is less than or equal to ₹ 10,00,000.	---	---
(b) For registration of OPC and small companies whose nominal share capital exceeds ₹ 10,00,000, the fee of ₹ 2000 with the following additional fees regulated according to the amount of nominal capital: For every ₹ 10,000 of nominal share capital or part of ₹ 10,000 after the first ₹ 10,00,000 and upto ₹ 50,00,000	---	200
2.(a) For registration of a company (other than OPC and small companies) whose nominal share capital is less than or equal to ₹ 10,00,000 at the time of incorporation.	---	---
(b) For registration of a company (other than OPC and small companies) whose nominal share capital exceeds ₹ 10,00,000, the fee of ₹ 36,000 with the following additional fees regulated according to the amount of nominal capital:	---	---
(i) for every ₹ 10,000 of nominal share capital or part of ₹ 10,000 after the first ₹ 10,00,000 upto ₹ 50,00,000.	300	---
	100	---

(ii) for every ₹ 10,000 of nominal share capital or part of ₹ 10,000 after the first ₹ 50,00,000 upto ₹ one crore. (iii) for every ₹ 10,000 of nominal share capital or part of ₹ 10,000 after the first ₹ 1 crore. Provided further that where the additional fees, regulated according to the amount of the nominal capital of a company, exceed a sum of rupees two crore and fifty lakhs, the total amount of additional fees payable for the registration of such company shall not, in any case, exceed rupees two crore and fifty lakhs.	75	---
3. For filing a notice of any increase in the nominal share capital of a company, the difference between the fees payable on the increased share capital on the date of filing the notice for the registration of a company and the fees payable on existing authorized capital, at the rates prevailing on the date of filing the notice: (a) For OPC and small companies whose nominal share capital does not exceeds ₹ 10,00,000 (b) For OPC and small companies, for every ₹ 10,000 of nominal share capital or part of ₹ 10,000 after the first ₹ 10,00,000 and upto ₹ 50,00,000. Other than OPC and small companies: (c) For increase in nominal capital of a company whose nominal share capital does not exceeds ₹ 1,00,000. (d) For increase in nominal capital of a company whose nominal share capital exceeds ₹ 1,00,000, the above fees of ₹ 5,000 with the following additional fees regulated according to the amount of nominal capital: (i) for every ₹ 10,000 of nominal share capital or part of ₹ 10,000 after the first ₹ 1,00,000 upto ₹ 5,00,000 (ii) for every ₹ 10,000 of nominal share capital or part of ₹ 10,000 after the first ₹ 5,00,000 upto ₹ 50,00,000 (iii) for every ₹ 10,000 of nominal share capital or part of ₹ 10,000 after the first ₹ 50,00,000 upto ₹ 1 crore.	--- --- 5000 400 300 100 75	2000 200 --- --- --- --- ---

(iv) for every ₹ 10,000 of nominal share capital or part of ₹ 10,000 after the first ₹ 1 crore. Provided further that where the additional fees, regulated according to the amount of the nominal capital of a company, exceed a sum of rupees two crore and fifty lakhs, the total amount of additional fees payable for the registration of such company shall not, in any case, exceed rupees two crore and fifty lakhs.		
4. For registration of any existing company, except such companies as are by this Act exempted from payment of fees in respect of registration under this Act, the same fee is charged for registering a new company.		
5. For submitting, filing, registering or recording any document by this Act required or authorised to be submitted, filed, registered or recorded: (a) in respect of a company having a nominal share capital of upto 1,00,000. (b) in respect of a company having a nominal share capital of ₹ 1,00,000 or more but less than ₹ 5,00,000. (c) in respect of a company having a nominal share capital of ₹ 5,00,000 or more but less than ₹ 25,00,000 (d) in respect of a company having a nominal share capital of ₹ 25,00,000 or more but less than ₹ 1 crore or more. (e) in respect of a company having a nominal share capital of ₹ 1 crore or more. Provided that in case of companies to be incorporated with effect from 26.01.2018 with a nominal capital which does not exceed rupees ten lakhs fee shall not be payable.	200 300 400 500 600	--- --- --- --- ---
6. For making a record of or registering any fact by this Act required or authorised to be recorded or registered by the Registrar: (a) in respect of a company having a nominal share capital of upto 1,00,000. (b) in respect of a company having a nominal share capital of ₹ 1,00,000 or more but less than ₹ 5,00,000.	200 300 400	--- --- ---

(c) in respect of a company having a nominal share capital of ₹ 5,00,000 or more but less than ₹ 25,00,000	500	---
(d) in respect of a company having a nominal share capital of ₹ 25,00,000 or more but less than ₹ 1 crore or more.	600	---
(e) in respect of a company having a nominal share capital of ₹ 1 crore or more.		
(II) In respect of a company not having a share capital:		
7. For registration of a company whose number of members as stated in the articles of association, does not exceed 20	---	
8. For registration of a company whose number of members as stated in the articles of association, exceeds 20 but does not exceed 200	5000	
9. For registration of a company whose number of members as stated in the articles of association, exceeds 200 but is not stated to be unlimited, the above fee of ₹ 5,000 with an additional ₹ 10 for every member after first 200		
10. For registration of a company in which the number of members is stated in the articles of association to be unlimited.	10000	
11. For registration of any increase in the number of members made after the registration of the company, the same fees as would have been payable in respect of such increase, if such increase had been stated in the articles of association at the time of registration: Provided that no company shall be liable to pay on the whole a greater fee than ₹ 10,000 in respect of its number of members taking into account the fee paid on the first registration of the company.		
12. For registration of any existing company except such companies as are by this Act exempted from payment of fees in respect of registration under this Act, the same fee as is charged for registering a new company.		

13. For filing or registering any document by this Act required or authorized to be filed or registered with the Registrar: Provided that in case of companies to be incorporated with effect from 26.01.2018 whose number of members as stated in the articles of association does not exceeds 20, fee shall not be payable.	200	
14. For making a record of or registering any fact by this Act required or authorized to be recorded or registered by the Registrar.	200	
(1) The above table prescribed for small companies (as defined under Section 2 (85) of the Act) and one person companies defined under Rule related to Chapter II read with Section 2 (62) of the Act shall be applicable provided the said company shall remain as said class of company for a period not less than one year from its incorporation. (2) The above table of fee shall be applicable for any such intimation to be furnished to the Registrar or any other officer or authority under Section 159 of the Act, filing of notice of appointment of auditors or Secretarial Auditor or Cost Auditor. (3) The above table of fee and calculation of fee as applicable for increase in authorised capital shall be applicable for revised capital in accordance with sub-section (11) of Section 233 of the Act, (after setting off fee paid by the transferor company on its authorised capital prior to its merger or amalgamation with the transferee company). (4) The above table of fee shall be applicable for filing revised financial statement or board report under Section 130 and 131 of the Act.		

B. Following Table of additional fee and higher additional fee (in certain cases) shall be applicable for delay in filing of forms other than for increase in Nominal Share Capital or forms under Section 92/137 of the Act or forms for filing charges

Table

Sl. No.	Period of Delays	Additional fee as a multiple of normal fees	Higher additional fee as a multiple of normal fees (for certain cases)
1.	Upto 15 days (Sections 139 and 157)	One time of normal fees	---
2.	More than 15 days and upto 30 days (Sections 139 and 157) and upto 30 days in remaining forms.	2 times of normal filing fees	3 times of normal filing fees
3.	More than 30 days and upto 60 days	4 times of normal filing fees	6 times of normal filing fees

4.	More than 60 days and upto 90 days	6 times of normal filing fees	9 times of normal filing fees
5.	More than 90 days and upto 180 days	10 times of normal filing fees	15 times of normal filing fees
6.	Beyond 180 days	12 times of normal filing fees	18 times of normal filing fees

Note 1: Higher additional fees shall be payable, if there is a delay in filing e-form INC-22, or e-form PAS-3, as the case may be, on two or more occasions, within a period of three hundred and sixty-five days from the date of filing of the last such belated e-form for which additional fee or higher additional fee, as the case may be, was payable.

Note 2: Wherever higher additional fee is payable, additional fee shall not be charged.

Note 3: e-form INC-22, or e-form PAS-3, as the case may be, filed prior to the commencement of the Companies (Registration Offices and Fees) Amendment Rules, 2022 shall not be reckoned for the purposes of determining higher additional fee.

C. For increase in authorised capital, the additional fees shall be applicable at the following rates:-

	Delay upto 6 months	Delay beyond 6 months
Slab	2.5% per month on the fees payable under para I.3 or II.12 of Table A above as the case may be.	3% per month on the fees payable under para I.3 or II.12 of Table A above as the case may be.
(1) The above fee table shall also be applicable for delay in filing application with Registrar under sub-section (11) of section 233 of the Act.		

D. For Forms under section 92 or 137:- (i) In case the period within which a document required to be submitted under section 92 or 137 of the Act expires after 30/06/2018, the additional fee mentioned in Table shall be payable -

Table

Sl. No.	Period of delay	Additional fee payable (in ₹)
01	Delay beyond period provided under Section 92(4) of the Act	One Hundred per day
02	Delay beyond period provided under Section 137(1) of the Act	One Hundred per day

(ii) In all other cases where the belated annual returns or balance sheet/financial statement which were due to be filed whether in the Companies Act, 1956 or the Companies Act, 2013 the following additional fee mentioned in Table shall be payable:-

Table

Sl. No.	Period of delay	Additional fee payable (in ₹) upto 30-6-2018
1	Upto 30 days	2 times of normal filing fees*
2	More than 30 days and upto 60 days	4 times of normal filing fees*
3	More than 60 days and upto 90 days	6 times of normal filing fees*
4	More than 90 days and upto 180 days	10 times of normal filing fees*
5	Beyond 180 days	12 times of normal filing fees*
	*plus ₹ 100 per day with effect from 1-7-2018	
Notes: (1) The additional fee shall also be applicable to revised financial statement or board's report under Sections 130 and 131 of the Act and secretarial audit report filed by the company secretary in practice under Section 204 of the Act. (2) The belated filing of documents/forms (including increase in nominal capital and delay caused thereon which were due to be filed whether in Companies Act, 1956 or the Companies Act, 2013 <i>i.e.</i> due for filing prior to notification of these fee rules, the fee payable at the time of actual filing shall be applicable.		

E. Fees for filing charge documents

(a) charges created or modified before 2nd November, 2018 and allowed to be filed within a period of three hundred days of such creation or six months from 2nd November, 2018, as the case may be, the following additional fees shall be payable:

Sl. No.	Period of delay	Additional fee applicable
1	Upto 30 days	2 times of normal fees
2	More than 30 days and upto 60 days	4 times of normal fees
3	More than 60 days and upto 90 days	6 times of normal fees
4	More than 90 days and upto 180 days	10 times of normal fees
5	More than 180 days	12 times of normal fees

(b) for charges created or modified on or after the 2nd November, 2018:-

(A) The following additional fees or *ad valorem* fees, as the case may be, shall be payable upto 31st July, 2019 by all companies:

Sl. No.	Period of delay	Additional/Ad valorem fees applicable
1	Upto 30 days	2 times of normal fees
2	More than 30 days and upto 60 days	4 times of normal fees
3	More than 60 days and upto 90 days	6 times of normal fees

(B) The following additional fees or *ad valorem* fees, as the case may be, shall be payable w.e.f. 1st August, 2019:

Sl. No.	Period of delay	Small companies and One Person Company	Other than Small companies and One Person Company
1	Upto 30 days	3 times of normal fees	6 times of normal fees
2	More than 30 days and upto 90 days	3 times of normal fees plus an <i>ad valorem</i> fee of 0.025% of the amount secured by the charge, subject to the maximum of one lakh rupees	6 times of normal fees plus an <i>ad valorem</i> fee of 0.05% of the amount secured by the charge, subject to the maximum of five lakh rupees

II. FEE ON APPLICATIONS (INCLUDING APPEAL) MADE TO CENTRAL GOVERNMENT UNDER SECTION 459 (2) OF THE COMPANIES ACT, 2013

1	For Application made	Other than OPCs and Small Companies	OPC and Small Companies
(i)	By a company having an authorized share capital of:		
	(a) Upto ₹ 25,00,000	2000	1000
	(b) More than ₹ 25,00,000 and upto ₹ 50,00,000	5000	2500
	(c) More than 50,00,000 and upto ₹ 5,00,00,000	10000	---
	(d) More than ₹ 5,00,00,000 and upto ₹ 10 crores	15000	---
	(e) More than ₹ 10 crores	20000	---

(ii)	By a company limited by guarantee but not having a share capital	2000	---
(iii)	By an Association or proposed company for issue of license under Section 8 of the Act	2000	---
(iv)	By a company having a valid license issued under Section 8 of the Act	2000	---
(v)	By a foreign company	5000	---
(vi)	For allotment of Director Identification Number (DIN) under Section 153 of the Act	500	500
(vii)	For surrender of Director Identification Number under Rule 11(f) of the Companies (Appointment and Qualification of Directors) Rules, 2014	1000	1000
(1) Every application to the Registrar of Companies filed by any person for reservation of name under sub-section (4) of Section 4 of the Companies Act, 2013, shall be accompanied with the fee of ₹ 1,000. (2) For every application made to the Regional Director (including appeal) or Registrar of Companies (except specifically stated elsewhere), Table of fees as above shall be applicable. Note: The separate fee schedule shall be prescribed under Sub-section (2) of Section 459 of the Act for applications to be filed before Tribunal.			

III. ANNUAL FEE PAYABLE BY A DORMANT COMPANY UNDER SUB-SECTION (5) OF SECTION 455 OF THE COMPANIES ACT, 2013

1	For Application made	Other than OPCs and Small Companies	OPCs and Small Companies
(i)	By a company having an authorized share capital of:		
	(a) Upto ₹ 25,00,000	2000	1000
	(b) More than ₹ 25,00,000 and upto ₹ 50,00,000	5000	2500
	(c) More than 50,00,000 and upto ₹ 5,00,00,000	10000	---
	(d) More than ₹ 5,00,00,000 and upto ₹ 10 crores	15000	---
	(e) More than ₹ 10 crores	20000	---
(ii)	By a company limited by guarantee but not having a share capital	2000	---

IV. FEE FOR INSPECTION AND PROVIDING CERTIFIED COPIES OF DOCUMENTS KEPT BY THE REGISTRAR UNDER SECTION 399 OF THE ACT

- (i) Under clause (a) of sub-section (1) of Section 399 of the Act – ₹ 100
- (ii) Under clause (b) of sub-section (1) of Section 399 of the Act
 - (a) For copy of Certificate of Incorporation – ₹ 100
 - (b) For copy or extract of other documents including hard copy of such document on computer readable media ₹ 25 per page.

V. FEE FOR REGISTRATION OF DOCUMENTS UNDER SECTION 385 OF THE ACT

₹ 6000 for each document.

VI. FEES FOR REMOVAL OF NAMES OF COMPANIES FROM THE REGISTRAR OF COMPANIES UNDER SECTION 248(2) OF THE ACT

₹ 5000

VII. FEE FOR FILING E- FORM DIR-3 KYC OR DIR 3 KYC –WEB UNDER RULE 12A OF THE COMPANIES (APPOINTMENT AND QUALIFICATION OF DIRECTORS) RULES, 2014

(i) Subject to serial number (iii) below, fee payable till the 30 th September of every financial year in respect of e-form DIR-3 KYC or DIR-3 KYC-WEB through web service, as the case may be, for the immediate previous financial year Note: For the financial year ended 31 st March 2019, no fee shall be payable in respect of e-form DIR-3 KYC or DIR-3 KYC-WEB through web service, till 14 th October, 2019.	---
(ii) Fee payable (in delayed case)	₹ 5000
(iii) Fee payable if the individual failed to file e-form DIR-3 KYC or DIR-3 KYC-WEB through web service, as the case may be, for the immediate previous financial year (in delayed case)	₹ 5000

VIII. FEE FOR FILING e-FORM ACTIVE UNDER RULE 25A OF THE COMPANIES (INCORPORATION) RULES, 2014

Fee payable till 15.06.2019 on e-form ACTIVE	---
Fee payable (in delayed case)	₹ 10000

INSTRUCTIONS

1. *Payment of fees* - Except as otherwise provided elsewhere, the table of fees annexed to the Companies (Registration Offices and Fees), Rules 2014, shall be payable in the following head.

(1) fees payable to the Registrar in pursuance of the Act or any rule or regulation made or notification issued thereunder shall be paid to the Registrar on any authorized bank by the Ministry of Corporate Affairs and acting as the agent of the Reserve Bank of India for credit under the following head, namely:

Major Head	Alphanumeric description	code	Account Code	Serial Code	Source category check digit
1475	Other general Economic service Regulation of joint stock companies		147500105	14750006	113
	(a) Registration fees		14750010599	14750032	114
	(b) Filing fees		14750010598	14750033	117
	(c) Inspection and copying fee		14750010597	14750034	112
	(d) Other fees		14750010596	14750035	119

(2) Where application is filed through electronic media or through any other computer readable media, the user may choose any one of the following payment options namely, (i) Credit Card; or (ii) Internet Banking; or (iii) Remittance at the Bank Counter or (iv) any other mode as approved by the Central Government. The requisite fee as specified in Companies (Registration Offices and Fees), Rules 2014 shall be payable through any of the accredited branches of the following Banks.

- (a) Punjab National Bank
- (b) State Bank of India
- (c) Indian Bank
- (d) ICICI Bank
- (e) HDFC Bank
- (f) Union Bank of India

(3) The fees payable to the Registrars may be paid bank drafts payable at drawn on banks, located at the same city or town as the office of the Registrar:

(4) Where a fee payable to the Registrar is paid through bank drafts as aforesaid it shall not be deemed to have been paid unless and until the relevant drafts are cashed and the amount credited.



7. MCA21 VERSION 3.0

In terms of Press Release No. 1695473, dated 05th February, 2021, Ministry of Corporate Affairs has announced key components of MCA21 Version 3.0. This Version will have additional modules for e-Adjudication, e-Consultation and Compliance Management.

MCA21 V3 Project is a technology-driven forward looking project, envisioned to strengthen enforcement, promote 'Ease of Doing Business', enhance user experience, facilitate seamless integration and data exchange among Regulators. The project will have Micro-services architecture with high scalability and capabilities for advanced analytics.

Aligned with global best practices and aided by emerging technologies such as **AI and ML**, MCA21 V3 is envisioned to transform the corporate regulatory environment in India.

Key Components of MCA21 V3.0

The key components of MCA21 V3.0 are as under:

1. **e-Scrutiny:** MCA is in process of setting up a Central Scrutiny Cell which will scrutinise certain Straight Through Process (STP) Forms filed by the corporates on the MCA21 registry and flag the companies for more in-depth scrutiny.
2. **e-Adjudication:** e-adjudication module, has been conceptualised to manage the increased volume of adjudication proceedings by the Registrar of Companies (RoC) and Regional Directors (RD) and will facilitate end to end digitisation of the process of adjudication, for the ease of users. It will provide a platform for conducting online hearings with stakeholders and end to end adjudication electronically.
3. **e-Consultation:** To automate and enhance the current process of public consultation on proposed amendments and draft rules etc., e-consultation module of MCA21 v3 will provide an online platform wherein, proposed amendments/draft legislations will be posted on MCA's website for external users/ comments and suggestions pertaining to the same in a structured digital format. Further, the system will also facilitate AI driven sentiment analysis, consolidation and categorization of stakeholders' inputs and creation of reports on the basis thereof, for reference of MCA.
4. **Compliance Management System (CMS):** CMS will assist MCA in identifying non-compliant companies/LLPs, issuing e-notices to the said defaulting companies/LLPs and generating alerts for internal users of MCA. CMS will serve as a technology platform/solution for conducting rule-based compliance checks and undertaking enforcement drives of MCA wherein e-notices will be issued by MCA for effective administration of corporates.

5. **MCA Lab:** As part of MCA21 V3, a MCA LAB is being set up, which will consist of corporate law experts. The primary function of MCA Lab will be to evaluate the effectiveness of Compliance Management System, e-consultation module, enforcement module, etc. and suggest enhancements to the same on an on-going basis. The Lab will help MCA in ensuring the correctness of results produced by these key modules in view of the dynamic corporate eco-system.

Additionally, MCA21 V3 will have a cognitive **chat bot enabled helpdesk, mobile apps, interactive user dashboards, enhanced user experience** using UI/UX technologies, and seamless data dissemination through APIs.



8. CASE STUDIES RELATING TO ETHICS

1. Case study

Facts of the case

CA. MP Iyer is a partner of M/s Swami and Sons Chartered Accountants, in Jaipur. He is the engagement partner (EP) for the statutory audit of XP Ltd.(XPL) for Financial year 2022-2023.

On an information received from the office of Registrar of Companies, in its investigation into the affairs of XPL, ROC noticed various professional misconducts on the part of the EP, who is partner of M/s Swami and Sons.

During its investigation, the ROC found that the company's books of accounts had been falsified and revenues inflated. The auditors had not performed their duties as "independent watchdogs". They had not verified the assets and inventories and had not qualified their reports.

Following the letter from ROC, NFRA took up the matter for investigation and initiated action under section 134(4) of the Companies Act, 2013 against EP, CA. MP Iyer.

During the investigation, NFRA prima facie found number of significant failures on the part of the EP during the audit of XPL for FY 2022-2023.

The EP was charged with Professional misconduct of:

- Failure to exercise due diligence and being grossly negligent in his conduct of the professional duties.
- Failure to obtain sufficient information necessary for expression of an opinion.
- Failure to invite attention to any requirement of generally accepted procedures of audit applicable to the circumstances.

Amongst the various failures, EP was charged with failure to evaluate the basis of arm's length pricing for the transactions entered with Related Parties as no documentation in this regard was found in the audit file.

During investigation, it came to the notice that more than 50% of the total sales for FY. 2022-2023 had been made to M/s Shambhu garments which is identified in the audit file as a partnership firm in which one of the partners, Prema das, wife of Bhima Das, is a Managing director of XPL, though identified as related party in the list of related parties in the audit file and the annual report for 2022-2023.

Requirement of the case study: Will the Transactions be treated as professional misconduct on the part of EP, CA MP Iyer and will he be liable to be charged under section 132(4) of the Companies Act?

Also, define the responsibility of the CFO of the Company in the given case.

Law and Compliance requirement

The statutory auditors (SAs), are appointed by the members of Companies under **section 139** of the Companies Act, 2013. The Statutory Auditors including the Engagement Partner and the Engagement Team which had conducted the audit are bound by the duties and responsibilities prescribed in the Act, the Rules made thereunder and the Code of Ethics.

According to **section 188** of the Companies Act, 2013, no company shall enter into any contract or arrangement with a related party except with the consent of the Board of Directors given by a resolution at a meeting of the Board and subject to such conditions as may be prescribed in the Law.

Provided also that nothing in this section shall apply to any of the transactions entered into by the company in its ordinary course of business other than transactions which are not on an arm's length basis.

The expression "arm's length transaction" means a transaction between two related parties that is conducted as if they were unrelated, so that there is no conflict of interest.

As per the legal requirement stated in **section 189 read with Rule 16 of the Companies (Meeting of Board and its Powers) Rules, 2014**, every company shall keep one or more registers giving separately the particulars of all contracts or arrangements to which section 188 applies, in such manner and containing such particulars as may be prescribed and after entering the particulars, such register or registers shall be placed before the next meeting of the Board and signed by all the Directors present at the meeting.

As per the facts, during investigation, it came to the notice of the Competent Authority that more than 50% of the total sales for FY. 2022-2023 had been made to M/s Shambhu garments which is identified in the audit file as a partnership firm in which one of the partners, is a Managing director of XPL, though she is identified as related party in the list of related parties in the audit file and the annual report for 2022-2023.

In the given case, EP failed to obtain sufficient information and in the warranted circumstances did not exercise due diligence, as she was required to evaluate the basis of arm's length pricing for the transactions entered with Related Parties. Also, no documentation in this regard was found in the audit file. Moreover, EP did not even obtain sufficient information for expressing his opinion.

As per the requirement of SA 550, when management made an assertion in the financial statements to the effect that a related party transaction was conducted on terms equivalent to those prevailing in an arm's length transaction, **the auditor needs to obtain sufficient appropriate audit evidence about the transaction.**

As no testing of the arm's length pricing in the audit file was evident, it is apparent that Engagement Partner did not comply with the requirements of SA 550, and has failed to obtain sufficient information warranted under the circumstances.

Conclusion:

EP CA. MP Iyer is guilty of professional misconduct under section 22 falling under clauses (7) and (8) of Part I of the Schedule II to the Chartered Accountants Act, 1949.

Whereas, CFO of the Company is under responsibility for overseeing the financial activities of the entire company will be held liable, if there is a default in compliance with provisions w.r.t. disclosures under the Companies Act, 2013.

If proper disclosure in line with legal requirement is not made, then the CFO (Key managerial personnel) would be liable for the action being taken against him under the Companies Act or under any other law for the time being in force.

Therefore, the CFO of the Company is not liable as details/particulars provided pertaining to related party in the list of related parties are there in the audit file and also taking place in the annual report for the year 2022-2023, but if the non-compliance would have been there, w.r.t. non-disclosure of the same, then CFO would have been guilty under Clause (1) of Part II of the Schedule II of the CA Act, 1949.

2. Case Study

Facts of the Case

ABC & Associates is a firm of Chartered Accountants. A Show Cause Notice under section 132(4) of the Companies Act, 2013, was served on the partners of the firm - CA. SG and CA. BC. They had been engaged for their services as Statutory Auditors of Hamper Limited for Financial year 2021-2022.

Pursuant to Securities and Exchange Board of India (SEBI)'s investigation regarding diversion of funds worth ₹ 1,000 crore from several subsidiaries of Primes Focus Limited, a listed company, NFRA initiated investigations under section 132(4) of the Act.

During its investigation, *inter alia* it was revealed that the Auditors of Hamper Limited for the FY 2021-2022 failed to meet the relevant requirements of the Standards of Auditing and the provisions of the Companies Act, 2013 and demonstrated serious lack of competence. The auditors had not performed their duties as "independent watchdogs". The Auditors of the company failed to maintain their independence from Hamper Limited by having audit and non-audit relationships with a large number of Prime Focus Group companies and the family members of the promoters.

The Engagement Partners (EP) - CA. SG and CA. BC and their firm was charged with Professional misconduct of:

- (a) Failure to disclose material fact known to the Auditors which is not disclosed in a financial statement, but disclosure of which is necessary in making financial statement where the Statutory Auditors are concerned with that financial statement in professional capacity.
- (b) Failure to exercise due diligence and being grossly negligent in the conduct of their professional duties.
- (c) Failure to obtain sufficient information necessary for expression of an opinion or its exceptions are sufficiently material to negate the expression of an opinion.
- (d) Failure to invite attention to any requirement from generally accepted procedures of audit applicable to the circumstances.

Amongst the various failures, EP was charged with failure to perform appropriate audit procedures while doing audit of related party transactions/balances in respect of which no documentation was found in the audit file.

During investigation, it came to the notice that the company had exceeded the limit of inter-company loans as provided under section 186 of the Companies Act, 2013. This resulted in material misstatement due to fraudulent diversion of funds and understating of related party loan.

Requirement of the Case study: Will the Transactions be treated as professional misconduct on the part of EP and will he be liable to be charged under section 132(4) of the Companies Act?

Law and Compliance requirement

Prime Focus Limited, a listed company has seven subsidiaries. One of its subsidiaries is Hamper Limited. The investigations by NFRA, *inter alia* revealed that the Auditors of Hamper Limited did not meet the relevant requirements of the Standards on Auditing and the provisions of the Companies Act, 2013 and demonstrated serious lack of competence.

Hamper Limited is a wholly owned subsidiary of Prime Focus Limited. Hamper Limited was incorporated in 2010 for carrying on the business of power generation but was yet to commence its operations (as on 31.3.2022). As per the Financial Statements of 2021-2022, Hamper Limited was neither engaged in the business of power generation nor had any revenue or expenditure related to power generation activities. The loans and advances given to the related parties (depicted as assets) of ₹ 517 crores constituted 94% of the total assets of ₹ 550 crores. The loans and advances taken from the related parties (depicted as Liabilities) of ₹ 570 crores constituted 95% of the total liabilities of ₹ 600 crores. These loans and advances were subsisting in the balance sheet of 2020-2021 also.

It was observed that Hamper Limited did not commence its operations, it had no physical assets, Work in progress, revenue, employee cost etc. and it invested in an infrastructure company to further its objective. The Management apprised that Hamper Limited had borrowed ₹ 570 crores from Prime Focus Limited, its holding company. Hamper Limited had given advances of ₹ 572 crore to Samrat Limited (an entity owned and controlled by the promoters of Prime Focus Limited) in 2018-2019. An amount of ₹ 55 crores was recovered in 2019-2020. The loans and advances to and from Prime Focus Limited and Samrat Limited were without charging any interest and without obtaining any security.

Hamper Limited had also taken a loan of ₹ 120 crores from a fellow subsidiary, Grand Limited. It was also informed that Hamper Limited had passed a special resolution in an Extraordinary General Meeting held on 1.5.2021 permitting borrowings upto 180 crore.

The Auditors of the company opined that:

1. They had collected Memorandum of Association and Articles of Association during their first year of audit of Hamper Limited, i.e. 2019-2020. They were the auditors of the company for 2020-2021 also. Hence, now it was not necessary to check these documents again as it was not their first year of engagement.
2. Section 186 of the Companies Act, 2013 allows the holding company to advance loans to its subsidiary company without further approvals, which implies that a subsidiary company can borrow from its holding company without restriction. They also admitted that the shareholders of Hamper Limited did not pass any special resolution as required under the Companies Act, 2013 (since the loan was given by Samrat Limited itself, approval of shareholders is implied to have been taken).
3. The loan taken from Grand Limited is within the limit of ₹ 180 crores which was approved by special resolution passed in Extraordinary General Meeting on 1.5.2021. They also informed that there is no legal requirement under the Companies Act, 2013 to report non-compliance with section 180 of the Act.
4. In respect of advances of ₹ 517 crores to Samrat Limited, the Auditors submitted that there is no need to have a written agreement for loan transaction with related parties. Also, since an amount of ₹ 55 crore has been recovered in 2019-2020, hence it did not warrant any comment regarding its recoverability.

Upon investigation by NFRA, the following observations were made:

1. There is no evidence in the Audit File that the Auditors had critically analysed the Financial Statements of Hamper Limited to understand the nature, operations, ownership, governance structure, loans and advances made and money borrowed by it. Hence, the Auditors were charged with failure to exercise professional judgement while planning and performing the Audit.
2. The Auditors ought to have questioned "Those Charged with Governance" (TCWG) and the Management about the authority under which the borrowing and lending activities were undertaken. They also should have examined the Memorandum of Association of Hamper Limited to ascertain its object clause that whether it can indulge in such borrowing and lending activities. Further, prudent Auditors are required to refresh their understanding about the entity during audit of second year and subsequent years also. There is no record in the Audit File about their understanding of the nature of business of Hamper Limited, its ownership,

governance structure etc. Had the auditors complied with their statutory duty as defined under SA 200 and 315, they would have unearthed that Hamper Limited had no business activities and was used by the promoters only for the purpose of diversion of funds.

3. The Auditors stand that a wholly owned subsidiary company is not required to take approval for taking loan from its holding company is misconceived as no such exemption is available under section 180(1)(c) of the Act, which requires special resolution of shareholders for borrowing in excess of the paid up share capital and free reserves.
4. In respect of the loan of ₹ 120 crore taken from Grand Limited, the understanding of Auditors is incomplete. The contention of Auditors that this ₹ 120 crore loan is within the limit of ₹ 180 crore passed in an Extraordinary General Meeting held on 1.5.2021 is not correct. This limit was already exceeded as the company already had borrowings of ₹ 570 crore subsisting.
5. In respect of the loan of ₹ 517 crore, it is to be noted that Samrat Limited and Hamper Limited did not have any business relation. Further, Hamper Limited is not in the business of Lending. Hence, the advance of such an amount that too without charging any interest is totally wrong. Also, the Auditors to have noticed the diversion of these funds to a promoter owned company. It was also noted that approvals required under section 179 and 186 of the Companies Act, 2013 were not obtained while giving the advances.
6. All these loans and advances were given without any business rationale, without authorisation and without any written agreements with counter parties.

Conclusion:

The Auditors had statutory duty to intimate the offence of fraud to the Central Government under section 143(12) of the Act. Disbursal of loans and advances without any business rationale and violating the provisions of the Act were indications of diversion of funds, which was a fraud on the company and ultimately fraud on the stakeholders of listed company i.e. Prime Focus Limited.

EP, CA. SG and CA. BC are liable under section 22, clauses (5), (6), (7), (8) and (9) of Part I of the Schedule II of the Chartered Accountants Act, 1949.

3. Case Study

Facts of the Case

Mr. Ravi promoted a company Tex-Mount Limited (TML) dealing in textile products about two-decades ago. He promoted this company along with two of his elder brothers and few friends, who are chemical engineers by profession.

During these two decades, TML has grown magnificently and it went public and its stocks were listed on leading stock exchanges. TML did well in the past and emerged as a major export unit but in recent years, the textile sector has witnessed stiff competition due to new entrants. The increased cost of the workforce and other input materials have also made the sector unprofitable. The recent lockdown has also affected the sector adversely. TML's bottom line for the current financial year is in the red.

TML was declaring dividends since very first year of its operations and is willing to continue the tradition, considering dividend to be a signalling effect to an investor for the purpose of valuation. Rate of dividend declared for the immediately preceding five years was 9%, 10%, 8%, 5% and 2% (9% being five years ago and 2% being the previous year) respectively. The management at TML decided to declare dividends out of the accumulated profits of previous years @ 7% on 14th June 2022.

On 14th July 2022, a portion of the dividend declared remains unpaid, due to operation of law. This amount has been transferred to Unpaid Dividend Account on 20th July 2022.

TML deals in exports and hence came under the scanner of the enforcement directorate which called for the financial statements and books of accounts of TML for scrutiny for the last 10 preceding financial years. In response to the said notice, TML furnished financial statements and books of accounts for last 8 immediately preceding financial years only, stating that as per its Article of Association, TML is required to maintain and keep the books of accounts only for 8 immediately preceding financial years and that too without any records of vouchers pertaining to such accounts.

CA. Dev was appointed as auditor of TML in his individual capacity at the 17th AGM, under section 139 of the Companies Act, 2013. He vacated the office of the auditor at the 23rd AGM and soon reappointed again at the 24th AGM.

Mr. Manoj, the CFO of the TML came across the following issues:

- (i) Whether the declaration of dividend @7% by TML leads to non-compliance of the provisions of the Companies Act, 2013?
- (ii) Is the vacation of CA. Dev as an auditor at 23rd AGM of TML and his reappointment at 24th AGM is Valid?
- (iii) Whether TML has violated the provisions of law regarding maintenance and preserving the Books of Account as per Act?
- (iv) Regarding declaration and distribution of dividend by TML, whether the company has violated the various timelines as provided in the Act?

Requirement of the Case study: Advise Mr. Manoj about the above issues and if any non-compliances have been done, what are the relevant remedies available with TML to make it fully compliant with the provisions of the Companies Act, 2013?

Observations and conclusions by Mr. Manoj, CFO of TML

- (i) **Declaration of dividend @7%** by TML is a non-compliance with the second proviso to Section 123. As per this proviso, the rate of dividend declared shall not exceed the average of the rates at which dividend was declared by the company in the immediately preceding three years. As per this, TML can declare the dividend but only up to 5% $[(8\% + 5\% + 2\%)/3]$ subject to satisfaction of other conditions as well.
- (ii) **Vacation of office of auditor by CA. Dev** at 23rd AGM and his reappointment at 24th AGM is contradictory with the provisions of section 139(2). According to Section 139(2), companies shall not appoint or re-appoint an individual as auditor for more than one term of five consecutive years and an individual auditor who has completed his term (i.e. one term of five consecutive years) shall not be eligible for re-appointment as auditor in the same company for five years from the completion of his term. Accordingly, CA. Dev has to vacate the office of the auditor at 22nd AGM and can be reappointed again only at 27th AGM.
- (iii) **TML has violated the provisions of law** because although it has preserved the books of account for 8 immediately preceding financial years but did not preserve the relevant vouchers pertaining to such books of accounts. As per section 128(5), the books of account of every company relating to a period of not less than eight financial years immediately preceding a financial year in respect of all the preceding years together with the vouchers relevant to any entry in such books of account shall be kept in good order.
- (iv) **TML has not violated the law** because the unpaid dividend has been transferred to the Unpaid Dividend Account on or before to 21st July 2022. According to Section 124, in case a dividend has been declared by a company but has not been paid or claimed within 30 days from the date of declaration, the company shall, within 7 days from the expiry of the 30 days, transfer the total amount of unpaid or unclaimed dividend to a special account called the Unpaid Dividend Account (UDA). Here, the dividend was declared by TML on 14th June 2022 and a portion of the dividend declared remains unpaid has been transferred to unpaid dividend account on 20th July 2022. This is within the timeline of 30+7 days.

4. Case Study

Fact of the case:

Y (Pvt.) Ltd (a subsidiary company of X Ltd., an unlisted public limited company) is a registered company under the provisions of the Companies Act, 2013 with its registered office in Mumbai. The company currently has 6 directors on its board consisting of 3 executive directors and 3 non-executive directors. The company is involved in software development and operating system consultancy and supply of business & other applications software for all platforms.

The company, Y (Pvt.) Ltd, during the course of its business transferred 333 equity shares in physical mode instead of transferring the same in demat mode as required under the provisions of Rule 9(A) (3) (a) of the Companies (Prospects and Allotment of Securities) Rules 2014 and it was given effect by the Board of Directors.

Being in violation of the provisions of Rules 9A (3) (a) of the Companies (Prospects and Allotment of Securities) Rules 2014, subsequently, the company had made good the non-compliance by getting the shares transferred to the demat account of the transferees in the demat mode from physical mode.

Action taken by the company

The company on realizing the violation committed in this matter decided to file a compounding application suo-moto admitting the violation. An application was filed by the company stating the fact that they had transferred 333 equity shares in physical mode before the securities were dematerialized thereby violating the provisions of Rule 9(A)(3)(a) of the Companies (Prospects and Allotment of Securities) Rules 2014. It requested the regulators to pass an appropriate order in this matter. The company also stated in the adjudication petition that the company had made good the non-compliance by getting the shares transferred to the demat account of the transferees in demat mode.

On adjudication of application for violation committed by the company, the Registrar of Companies issued a personal hearing notice to the company and its directors directing them to appear before him.

Reply received from the non-executive directors

The regulators had sent the notice to all company's directors as per the records available on the MCA Portal. The non-executive directors who received the notice from the regulators replied through a common e-mail stating that they are non-executive directors of the company and hence would not come under the ambit of officer in default of the company.

During Adjudication, on day of hearing:

The company authorized practicing company secretary to appear on behalf of the company and its directors representing the company and stated the following:-

- (i) The practicing company secretary **admitted the default on behalf of the company and its directors.**
- (ii) The practicing company secretary further stated that the **company/ its directors had made good the non-compliance** by getting the shares transferred to the demat account of the transferees in demat mode as had been mentioned in the adjudication application.

Requirements of the case: 1. To examine whether the Rule 9(A) (3) (a) of the Companies (Prospects and Allotment of Securities) Rules 2014 shall apply to Y (Pvt.) Ltd.

2. Whether it is justifiable that non-executive directors are not liable to be charged, though they were part of the management on the day of the default and will they be penalised?

3. As the default was admitted by the company and its directors before the Adjudicating Authority and by doing good the non-compliance, will this release them from the liability of non-compliance?

Observations and conclusions by the Adjudicating Officer**(1) Applicability of 9(A) (3) (a) of the Companies (Prospects and Allotment of Securities) Rules 2014 to this company**

As per the provisions of the Companies Act 2013, section 2 (71) defines a public company as "public company" means a company which (i) is not a private company and (ii) has a minimum paid up share capital as may be prescribed. Provided that a company which is a subsidiary of a company, not being a private company, shall be deemed to be a public company for the purposes of this Act even where such subsidiary company continues to be a private company in its articles of association.

From the above, one can come to a conclusion that if a private company which is a subsidiary of a public company will be treated as a public company only and all attributes and characteristics of a public company get attached to it even it continues to be private company in its articles of association.

In view of foregoing discussions, Y (Pvt.) Ltd. being a subsidiary company of a public limited company (i.e. X Ltd.) is considered as a deemed unlisted public company and therefore Rule 9(A)

(3) (a) of the Companies (Prospects and Allotment of Securities) Rules 2014 applies to Y (Pvt.) Ltd. though it is a private limited company.

Every unlisted public company shall have to issue the security only in dematerialized form and also facilitate dematerialization of all its existing securities in accordance with provisions of the Depositories Act 1996 and regulations made thereunder.

With respect to applicability of these provisions to a private company, it may be noted that if a private company is subsidiary of a public company, then such private company is considered to be a deemed public company and such private company shall have to comply with this provision specified in Rule 9(A) (3) (a) of the Companies (Prospects and Allotment of Securities) Rules 2014.

(2) After going through the adjudication petition filed by the company and its directors and also upon hearing the submissions made during the personal hearing by the company and its directors admitting the violation, the Adjudicating Officer, came to the conclusion that the company and its directors had committed the violation of Rule 9A (3) (a) of Companies (Prospectus and Allotment of Securities) Rules 2014 attracting the penalty.

Any non-compliance/ default committed by the company in complying with the provisions of Rule 9(A) (3) (a) of the Companies (Prospects and Allotment of Securities) Rules 2014 would attract penal action in case of a private company which is a subsidiary of a public company. It shall have to comply with the provisions of Rule 9(A)(3)(a) of the Companies (Prospectus and Allotment of Securities) Rules 2014. In this particular case, the company and its executive directors were penalized by the regulators while the non-executive directors were kept out of the purview of the default since they were not involved in the day-to-day activities / operations of the company.

The Adjudicating Officer came to a conclusion that the company had 3 non-executive directors on its board who were not to be charged for the violations since the company had 3 executive directors who were responsible for the day-to-day affairs and activities of the company, were to be penalised.

Accordingly, the Adjudicating Officer would pass an order for the violation committed by the company and 3 executive directors.

(3) Adjudicating authority defined that, as per the law, the company needs to ensure the applicable compliances in order to avoid penal action from the regulators.

1. The Companies Act 2013
2. The Companies (Prospectus and Allotment of Securities) Rules 2014

3. The Companies (Adjudication of Penalties) Rules 2014

Admission of default by the company before the Adjudicating Authority and by doing good the non-compliance will not discharge the company and officers from their responsibilities. In view this, justice shall be met if a reasonable punishment is levied.

Following order shall be passed by the Adjudicating Officer after having considered the facts and circumstances of the case and the submission made by the company, director, KMP's through their authorized representative, in view of the violation of Rule 9A(3)(a) of Companies(Prospectus and Allotment of Securities) Rules 2014 and in exercise of the powers vested under section 454(3) of the Companies Act 2013, imposed penalty in the following manner on the company and all the officers in default.

Serial number	Company / Directors	Penalty imposed
1	Company	10,000
2	Director-1	10,000
3	Director-2	10,000
4	Director-2	10,000
Total Penalty		40,000

TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. The nomenclature MCA21 reflects -----
 - (a) that the portal contains 21 e-Forms to be filed electronically by a company during any financial year.
 - (b) that it is linked with Section 21 of the Companies Act, 2013.
 - (c) that MCA is capable of fulfilling the aspirations of its stakeholders in the 21st century.
 - (d) that it contains 21 standardised features.
2. Electronic form for the specified purposes shall be:
 - (a) exclusive, or in the alternative or in addition to the physical form.
 - (b) inclusive, or in the alternative or in addition to the physical form.
 - (c) extensible or in the alternative or in addition to the physical form.
 - (d) inclusive, or in the alternative or complementary to the physical form.
3. SRN stands for:
 - (a) Service Request Notice
 - (b) Service Reporting Number
 - (c) Signature Request Notice
 - (d) Service Request Number
4. Apoorva Medicines Limited shall be required to file financial statements through XBRL:
 - (a) If it has a paid-up capital of ₹ 5 crores and above.
 - (b) If it has a turnover of ₹ 75 crores and above.
 - (c) Both (a) and (b).
 - (d) Neither (a) nor (b).
5. XBRL stands for:
 - (a) eXtension Business Reporting Language
 - (b) eXtensible Business Reporting Language
 - (c) eXclusive Business Reporting Language
 - (d) eXtended Business Reporting Language

Descriptive Questions

1. Discuss some of the salient features of MCA21.
2. (i) Raashi, one of the directors of Puneet Mechanics Private Limited, submitted e-Form ADT-3 (Notice of Resignation by the Auditor) through e-mail. Whether the same constitutes valid e-filing.
(ii) Which companies are exempted from filing of financial statements under the Companies (Filing of Documents and Forms in Extensible Business Reporting Language) Rules, 2015?
3. State the process involved in e-Filing.

ANSWER KEYS

Answer to Multiple Choice Questions

1.	c	2.	a	3.	d	4.	a	5.	b

Descriptive Answers

1. Some of the salient features of MCA21 are as under:
 1. *Online Portal:* It is the online portal of the Ministry of Corporate Affairs (MCA). It has made all company related information accessible to various stakeholders and the general public.
 2. *Convenient:* It provides the services on the basis of anywhere and anytime with speed and certainty.
 3. *Easy and secure access:* It provides easy and secure access of the MCA services to various stakeholders.
 4. *Full Automation:* It has fully automated all the processes, thus making India globally competitive.
 5. *Multiple Payment Options:* It provides multiple options to make online payment.
 6. *SRN:* It provides Service Request Number (SRN) which enables the stakeholders to track their service request.
2. (i) Submission of e-Form ADT-3 (Notice of Resignation by the Auditor) through e-mail by Raashi, one of the directors of Puneet Mechanics Private Limited, does not constitute valid e-filing. Therefore, she needs to avoid such kind of a submission.

- (ii) According to second Proviso to Rule 3 (1) of the Companies (Filing of Documents and Forms in Extensible Business Reporting Language) Rules, 2015 following companies are exempted from filing of financial statements under these rules:
 - (a) Non-banking financial companies;
 - (b) Housing Finance Companies;
 - (c) Companies engaged in the business of Banking;
 - (d) Companies belonging to Insurance sector.
- 3. The process involved in e-Filing of various documents is stated as under:
 - 1. One-time registration of the user at the on-line Portal of MCA21 for creating his personalised login ID.
 - 2. Registration of Digital Signature Certificate (DSC).
 - 3. Downloading of e-form and instruction kit, if required.
 - 4. After downloading, the user is required to complete the e-form by filling it either online or off-line.
 - 5. On-line filling requires active internet connection.
 - 6. The e-Forms can be filled-in and signed digitally using an Acrobat Reader.
 - 7. The user can use “pre-fill” option. This will fill-up certain fields of e-forms automatically.
 - 8. The user can do “automated pre-scrutiny” of e-form. This will ensure that the e-Form is complete in all respects and is good for e-filing.
 - 9. The user may also attach supporting documents, if applicable.
 - 10. After completion, the user is required to sign the e-form using the Digital Signature Certificate (DSC).
 - 11. Now, the e-form is ready for e-filing at the MCA21 portal using specialized functionality that is provided at the portal.
 - 12. If the e-Form is correct in all respects, the user can proceed to the next step of making payment.
 - 13. For making payment of applicable fee, the user will be asked to choose any one of the following methods of payment:
 - Credit Card/Debit Card
 - Internet Banking

- NEFT
- Physical Challan (*i.e.* at Bank counter)
- Pay Later

In case payment mode is Credit Card/Debit Card, Internet Banking, etc. the payment will be made instantly. System will generate a receipt that the user can retain as a part of his records.

In the case of challan payment, a fully completed challan will be generated by the system that can be printed by the user and taken to any of the nearest authorized branch. He may choose to pay either through cash (limits as stipulated by Law will be applicable) or through a local cheque or DD. The acknowledged copy of the challan will serve as the receipt.

Once the user has made the payment in the Bank following the challan payment system, the filing shall be complete. Based on confirmation of payment by the bank to the MCA21 system, the document will be transmitted to the Back Office for further processing.

In case of Pay Later, e-form can be uploaded on MCA portal in one step and make the payment at later point of time using the online payment mode *i.e.*, Credit Card/Debit Card, Internet Banking, etc. An e-challan generated at the time of uploading e-form contains the validity date within which payment shall be made by the user.

14. e-Filing will be completed once the necessary payment is remitted either through electronic payment means or through the challan-based method.
15. The user will also be provided a facility at MCA21 portal to check if the e-filing has been completed successfully.

[illegible]

SET
A
**SELF-PACED
STUDY MATERIAL**
**CORPORATE AND
ECONOMIC LAWS**
MODULE 2 OF 2



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CONTENTS

PART I: CORPORATE LAWS

SECTION A: COMPANY LAW

MODULE – 1

- Chapter 1: Appointment and Qualifications of Directors
- Chapter 2: Appointment and remuneration of Managerial Personnel
- Chapter 3: Meetings of Board and its powers
- Chapter 4: Inspection, inquiry and Investigation
- Chapter 5: Compromises, Arrangements and Amalgamations
- Chapter 6: Prevention of Oppression and Mismanagement
- Chapter 7: Winding Up
- Chapter 8: Miscellaneous Provisions
- Chapter 9: Compounding of offences, Adjudication, Special Courts, National Company Law Tribunal and Appellate Tribunal
- Chapter 10: e-Filing

SECTION B: SECURITIES LAWS

MODULE – 2

Chapter 1: The Securities Exchange Board of India Act, 1992 and SEBI (Listing Obligations and Disclosure Requirement) Regulations, 2015, SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018, SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 2011, SEBI (Prohibition of Insider Trading) Regulations, 2015.

PART II: ECONOMIC LAWS

- Chapter 1: The Foreign Exchange Management Act, 1999
- Chapter 2: The Foreign Contribution Regulation Act, 2010
- Chapter 3: The Insolvency and Bankruptcy Code, 2016

DETAILED CONTENTS: MODULE – 2

SECTION B: SECURITIES LAWS

Page No.

CHAPTER 1: SEBI Act, 1992, SEBI (LODR) Regulations, 2015, SEBI (ICDR) Regulations, 2018, SEBI (SAST) Regulations, 2011 and SEBI (PIT) Regulations, 2015

1.	Introduction	1.2
2.	Important definitions	1.2
3.	Establishment of the Securities and Exchange Board of India.....	1.3
4.	Powers and Functions of SEBI.....	1.6
5.	Board to regulate or prohibit issue of prospectus, offer document or advertisement soliciting money for issue of securities	1.12
6.	Collective investment scheme.....	1.12
7.	Power to issue directions.....	1.13
8.	Investigation.....	1.14
9.	Cease and desist proceedings	1.17
10.	Registration Certificate	1.18
11.	Prohibition of manipulative and deceptive devices, insider trading and substantial acquisition of securities or control	1.19
12.	Finance, Accounts and Audit	1.20
13.	Penalties and Adjudication	1.21
14.	Establishment, Jurisdiction, Authority and Procedure of Securities Appellate Tribunal (SAT)	1.32
15.	Miscellaneous.....	1.39

SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015

1.	Scope	1.49
2.	Introduction	1.50

3.	Regulation.....	1.50
4.	Common Obligations of Listed Entities.....	1.56
5.	Quarterly Compliances	1.57
6.	Prior Intimation of Board Meeting	1.58
7.	Annual / Yearly Compliances	1.60
8.	Corporate Governance	1.61
9.	Types of Committees under LODR Regulations	1.65

SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018

1.	Introduction	1.70
2.	Other Relevant Definitions	1.71
3.	Applicability of the Regulations	1.72
4.	Initial Public Offer on Main Board.....	1.74
5.	Issue of Convertible Debt Instruments and Warrants	1.79
6.	Promoters' Contribution	1.81
7.	Lock-In and Restrictions on Transferability.....	1.83
8.	Disclosures in and Filing of Offer Documents	1.86
9.	Pricing	1.89
10.	Issuance Conditions and Procedure.....	1.90
11.	Miscellaneous	1.94
12.	Further Public Offer	1.97
13.	Issue of Convertible Debt Instruments and Warrants	1.100
14.	Promoters' Contribution	1.103
15.	Lock-In and Restrictions on Transferability.....	1.105
16.	Disclosures in and Filing of Offer Documents	1.107
17.	Pricing	1.110
18.	Issuance Conditions and Procedure.....	1.111
19.	Miscellaneous	1.120

THE SECURITIES AND EXCHANGE BOARD OF INDIA (SUBSTANTIAL ACQUISITION OF SHARES AND TAKEOVERS) REGULATIONS, 2011

1.	Introduction	1.123
2.	Relevant terminologies	1.123
3.	Substantial Acquisition of Shares, Voting Rights or Control	1.126
4.	Obligations	1.128
5.	Disclosures of Shareholding and Control.....	1.133

SECURITIES AND EXCHANGE BOARD OF INDIA (PROHIBITION OF INSIDER TRADING) REGULATIONS, 2015

1.	Definitions	1.136
2.	Restrictions on Communication and Trading by Insiders	1.138
3.	Disclosures of Trading by Insiders	1.145
4.	Codes	1.147
	Test Your Knowledge	1.150

PART II: ECONOMIC LAWS**CHAPTER 1: THE FOREIGN EXCHANGE MANAGEMENT ACT, 1999**

1.	Introduction	1.2
2.	Preamble, Extent, Application and Commencement of FEMA, 1999	1.3
3.	Definitions	1.4
4.	Residential status under FEMA	1.7
5.	Regulation and Management of Foreign Exchange	1.12
6.	Authorised Person	1.78
7.	Contraventions and Penalties in Brief	1.81
8.	Compounding of Offences.....	1.84
9.	Adjudication and Appeal	1.84
10.	Directorate of Enforcement	1.86

11.	Miscellaneous.....	1.87
	Test Your Knowledge	1.90

CHAPTER 2: THE FOREIGN CONTRIBUTION REGULATION ACT, 2010

1.	Introduction	2.2
2.	Important Definitions	2.4
3.	Regulation of Foreign Contribution and Foreign Hospitality	2.9
4.	Registration	2.17
5.	Accounts, Intimation, Audit and Disposal of Assets, etc.	2.28
6.	Adjudication.....	2.31
7.	Appeal & Revision	2.32
8.	Offences and Penalties	2.34
9.	Miscellaneous.....	2.37
	Test Your Knowledge.....	2.39

CHAPTER 3: THE INSOLVENCY AND BANKRUPTCY CODE, 2016

1.	Introduction	3.2
2.	Important Definitions	3.11
3.	Corporate Insolvency Resolution Process.....	3.21
4.	Liquidation Process	3.63
	Test your knowledge	3.66

CHAPTER

1

THE SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992 SEBI (LODR) REGULATIONS, 2015, SEBI (ICDR) REGULATIONS, 2018, SEBI (SAST) REGULATIONS, 2011, SEBI (PIT) REGULATIONS, 2015



LEARNING OUTCOMES

By the end of this chapter, students will be able to-

- ❑ Describe the role, powers and functions of the Securities and Exchange Board of India
- ❑ Determine how the SEBI regulates the capital markets in India under a resolution of the Government of India
- ❑ Specify the prohibition of manipulative and deceptive devices, insider trading and substantial acquisition of securities or control
- ❑ Lay down the penalties and adjudication and identify the establishment, jurisdiction, authority and procedure of Appellate Tribunal.
- ❑ Elucidate the significant regulations governed by the SEBI(Listing Obligations and Disclosure Requirement) Regulations, 2015, SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018, SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 2011, SEBI (Prohibition of Insider Trading) Regulations, 2015



1. INTRODUCTION

The Securities and Exchange Board of India was established in 1988. It got legal character in 1992. SEBI was primarily set up to regulate the activities of the merchant banks, to control the operations of mutual funds, to work as a regulator of the stock exchange activities and to act as a regulatory authority of new issue activities of companies. The reason the SEBI was constituted was because before the SEBI the law relating to the securities market in India was contained in different enactments like Companies Act, 1956, Securities Contract (Regulation) Act, 1956, and the Capital Issues (Control) Act, 1947. Then, at times when the capital market witnessed tremendous growth, it was found, that the legislation was scattered in different laws and administrative agencies did not have proper manpower or expertise to deal with the investors. Even there was no monitoring or prosecuting machinery to check malpractices, insider trading, etc. Then, Government of India decided to set up an agency or regulatory body known as Securities Exchange Board of India (SEBI). SEBI was first established in 1988 as a non-statutory body for regulating the securities market. It became an autonomous body on 30 January 1992 and was accorded statutory powers with the passing of the SEBI Act 1992 by the Indian Parliament.

In the year of 1995, the SEBI was given additional statutory power by the Government of India through an amendment to the Securities and Exchange Board of India Act, 1992.

The prime objective of the SEBI Act, 1992 are:

1. Protecting the interests of the investors in securities;
2. Promoting the development of, and;
3. Regulating, the securities market and for matters connected therewith or incidental thereto.

SEBI as the watchdog of the securities market has an important and crucial role in regulating the market participants and perform the aforementioned three duties in accordance with the regulatory norms. The preamble of the SEBI describes the basic functions of the SEBI as '*...to protect the interest of investors in the securities and to promote the development of, and to regulate the securities market and for matters connected therewith*'.

This SEBI Act deemed to have come into force on the 30th day of January 1992 and extended to whole of India as per Section 1 of the SEBI Act, 1992.



2. IMPORTANT DEFINITIONS

According to section 2 of the SEBI Act, 1992, following are some of the important definitions of terms used in the Act-

Board means the Securities and Exchange Board of India established under section 3; [Section 2(1) (a)]

Collective investment scheme means any scheme or arrangement which satisfies the conditions specified in section 11AA [Section 2(1)(ba)]

Judicial Member means a Member of the Securities Appellate Tribunal appointed under sub-section (1) of section 15MA and includes the Presiding Officer; [Section 2(1)(db)]

Member means a member of the Board and includes the Chairman; [Section 2(1)(e)]

Regulations means the regulations made by the Board under this Act; [Section 2(1)(h)]

Reserve Bank means the Reserve Bank of India constituted under section 3 of the Reserve Bank of India Act, 1934 [Section 2(1)(ha)]

Securities has the meaning assigned to it in section 2 of the Securities Contracts (Regulation) Act, 1956 [Section 2(1)(i)]

Technical Member means a Technical Member appointed under sub-section (1) of section 15MB. [Section 2(1)(j)]

(2) Words and expressions used and not defined in this Act but defined in the Securities Contracts (Regulation) Act, 1956 or the Depositories Act, 1996, shall have the meanings respectively assigned to them in that Act.



3. ESTABLISHMENT OF THE SECURITIES AND EXCHANGE BOARD OF INDIA

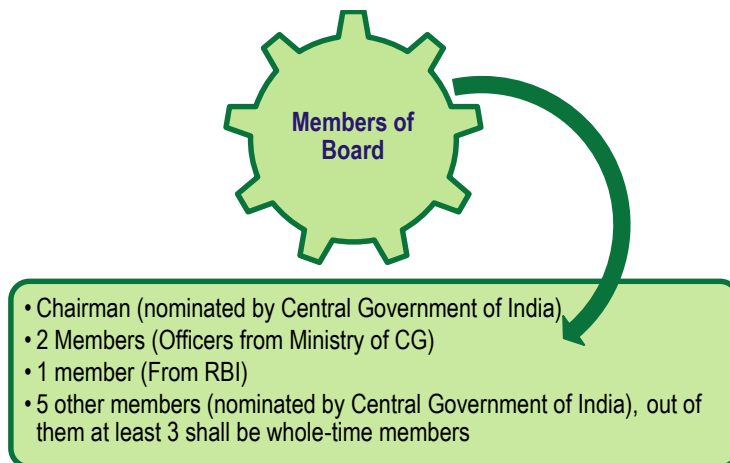
Establishment and incorporation of Board [Section 3]

SEBI (hereinafter called 'the Board') has been established as-

- a body corporate
- having perpetual succession and a common seal,
- with powers to acquire, hold and dispose of property, both movable and immovable, and
- to contract as also to sue or be sued by the name of SEBI.
- The head office of the Board shall be at Mumbai. Further the Board may establish offices at other places in India.

Management of the Board [Section 4]

The SEBI Board is managed by its members (appointed by the Central Government). The Board consists of the following members:



The Chairman and the all the other members as referred in the section, shall be persons of ability, integrity and standing who have shown capacity in dealing with problems relating to securities market or have special knowledge or experience of law, finance; economics, accountancy, administration or in any other discipline which, in the opinion of the Central Government, shall be useful to the Board [Section 4(5)].

The general superintendence, direction and management of the affairs of the Board shall vest in a Board of Members, which may exercise all powers and do all acts and things, which may be exercised or done by the Board. [Section 4(2)]

Term of office and conditions of service of Chairman and members of the Board [Section 5]

The term of office and other conditions of service of Chairman and the Members appointed in section 4(1)(d) (i.e., the 5 members appointed by Central Government) shall be such as may be prescribed by rules made under the Act.

Right to termination: The Central Government will have the right to terminate the services of the Chairman or the Members appointed in section 4(1)(d) (i.e., the 5 members appointed by Central Government) at any time before the expiry of their tenure-

by giving not less than three months' notice in writing

OR

three months' salary and allowance in lieu thereof

The Chairman and all the other members (not just the 5 members appointed by CG) shall have the right to relinquish office at any time before the expiry of their tenure by giving a notice of three months in writing to the Central Government.

Term of office: As per the rules framed in this regard, the Chairman and Whole time Members shall hold office for such period, not exceeding 5 years, as many be specified in the order of his appointment; but he shall be eligible for reappointment;

Provided that no person shall hold office as the Chairman or a Member after he attains the age of sixty-five years.

Removal of Members of the Board [Section 6]

The Central Government shall remove a member from office if he:

-  at any time has been adjudicated as insolvent;
-  has been declared by a competent court to be of unsound mind;
-  has been convicted of an offence which in the opinion of the Central Government, involves a moral turpitude.
-  has in the opinion of the Central Government so abused his position as to render his continuance in office detrimental to the public interest.

Provided that no member shall be removed under this clause unless he has been given a reasonable opportunity of being heard in the matter

Meetings of the Board [Section 7]

The Board shall meet at such times and places and shall observe such rules of procedure in regard to the transaction of business at its meetings (including quorum at such meetings) as may be provided by regulations.

In the absence of the Chairman: If for any reason, Chairman is unable to attend a meeting, any member chosen by the members present from amongst themselves shall preside over the meeting.

Decision by majority vote: All questions which come up before any meeting shall be decided by majority vote of the members present and the Chairman or the presiding member will have a second or casting vote, in the event of equality of votes.

Member not to participate in meetings in certain cases [Section 7A]

Any member-

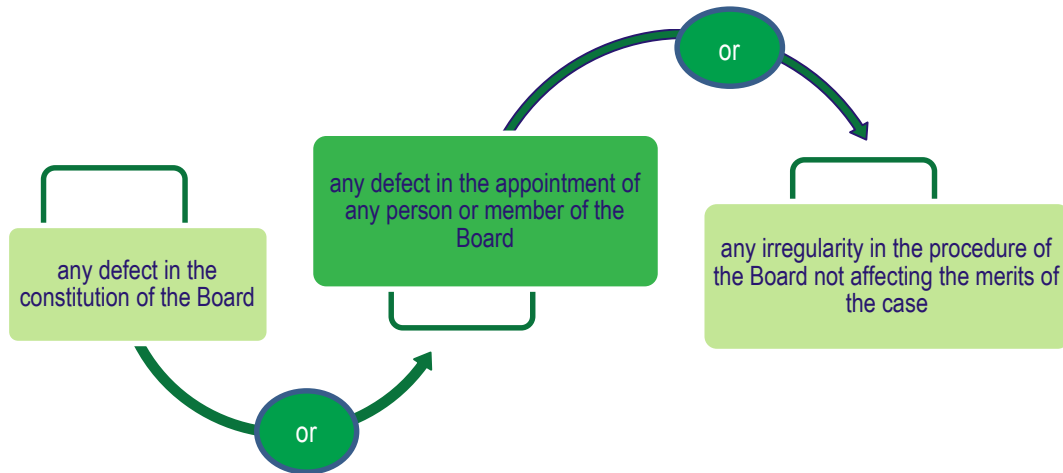
- who is a director of a company, and
- who as such director has any indirect pecuniary interest in any matter coming up for consideration at a meeting of the Board,

shall, disclose (as soon as possible after relevant circumstances have come to his knowledge) the nature of his interest at such meeting and such disclosure shall be recorded in the proceedings of

the Board, and the member shall not take any part in any deliberation or decision of the Board with respect to that matter.

Vacancies, etc., not to invalidate proceedings of the Board [Section 8]

- Any vacancy in the Board shall not invalidate any of the acts or proceeding of the Board. Similarly, the following events shall not invalidate any act or proceeding of the Board-



4. POWERS AND FUNCTIONS OF SEBI [SECTION 11]

Subject to the provisions of this Act, it shall be the duty of the Board to protect the interest of investors in securities and to promote the development of, and to regulate the securities market, by such measures as it thinks fit.

The measures may provide for:

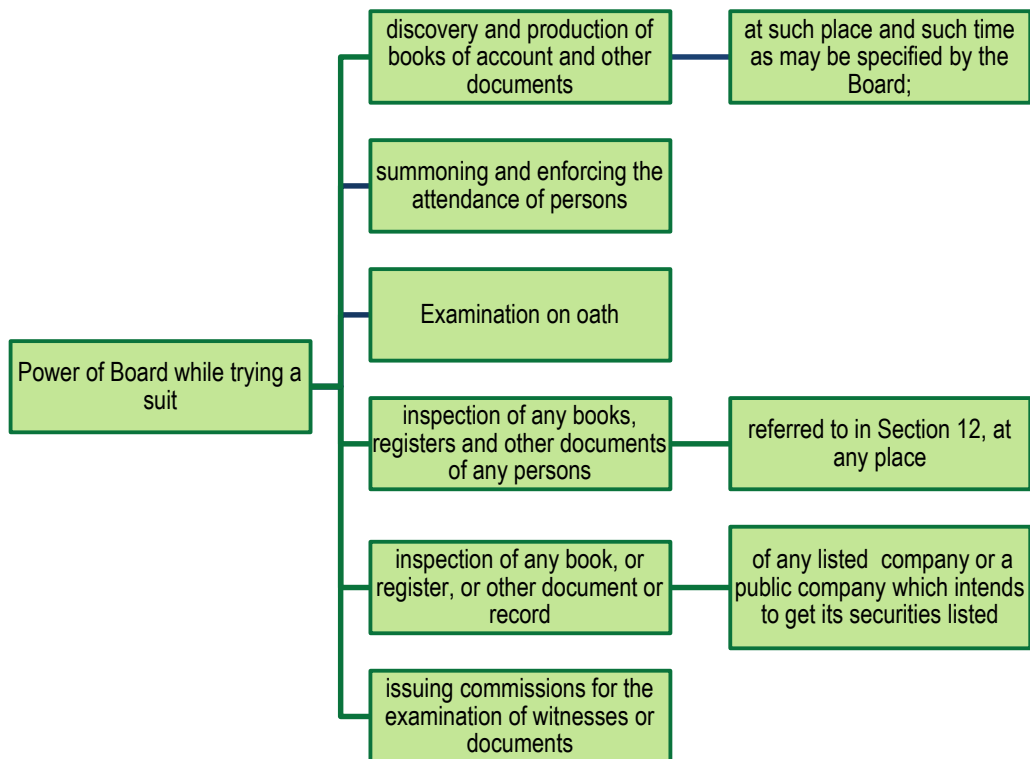
- (a) **regulating the business** in stock exchanges and any other securities markets;
- (b) **registering and regulating the working of stock brokers, sub - brokers**, share transfer agents, bankers to an issue, trustees of trust deeds, registrars to an issue, merchant bankers, underwriters, portfolio managers, investment advisers and such other intermediaries who may be; associated with securities markets in any manner;
- (ba) **registering and regulating the working of the depositories, participants**, custodians of securities, foreign institutional investors, credit rating agencies and such other intermediaries as the Board may, by notification, specify in this behalf.
- (c) **registering and regulating the working of venture capital funds and collective investment schemes**, including mutual funds;
- (d) **promoting and regulating self-regulatory organisations**;

- (e) **prohibiting fraudulent and unfair trade practices** relating to securities markets;
- (f) **promoting investors' education and training** of intermediaries' of securities markets;
- (g) **prohibiting insider trading** in securities;
- (h) **regulating substantial acquisition of shares** and take-over of companies;
- (i) **calling for information from undertaking inspection**, conducting inquiries and audits of the stock exchanges, mutual funds, other persons associated with securities market, intermediaries and self-regulatory organizations in the securities market
- (ia) **calling for information and records from any person** including any bank or any other authority or board or corporation established or constituted by or under any Central or State Act which, in the opinion of the Board, shall be relevant to any investigation or inquiry by the Board in respect of any transaction in securities;
- (ib) **calling for information from, or furnishing information to, other authorities**, whether in India or outside India, having functions similar to those of the Board, in the matters relating to the prevention or detection of violations in respect of securities laws, subject to the provisions of other laws for the time being in force in this regard:

Provided that the Board, for the purpose of furnishing any information to any authority outside India, may enter into an arrangement or agreement or understanding with such authority with the prior approval of the Central Government;
- (j) **performing such functions and exercising such powers under the provisions of the Securities Contracts (Regulation) Act, 1956**, as may be delegated to it by the Central Government.
- (k) **levying fees or other charges** for carrying out the purposes of this section.
- (l) **conducting research** for the above purposes;
- (la) **calling from or furnishing to any such agencies**, as may be specified by the Board, such **information** as may be considered necessary by it for the efficient discharge of its functions.
- (m) **performing such other functions** as may be prescribed.

Power with respect to inspection of books and Documents: Further, the Board may take measures to undertake inspection of any book, or register, or other document or record of any listed public company or a public company which intends to get its securities listed on any recognised stock exchange where the Board has reasonable grounds to believe that such company has been indulging in insider trading or fraudulent and unfair trade practices relating to securities market.

Board are vested with same power as that of civil court: The Board shall have the same powers as are vested in a civil court under the Code of Civil Procedure, 1908 while trying a suit, in respect of the following matters, namely:



Passing of an order by an Board: The Board may, by an order, for reasons to be recorded in writing, in the interests of investors or securities market, take any of the following measures, either pending investigation or inquiry or on completion of such investigation or inquiry, namely:—

- suspend the trading** of any security in a recognised stock exchange;
- restrain persons from accessing** the securities market and prohibit any person associated with securities market to buy, sell or deal in securities;
- suspend any office-bearer** of any stock exchange or self-regulatory organization from holding such position;
- impound and retain** the proceeds or securities in respect of any transaction which is under investigation;
- attach**, for a period not exceeding ninety days, bank accounts or other property of any intermediary or any person associated with the securities market in any manner involved in violation of any of the provisions of this Act, or the rules or the regulations made thereunder:

Provided that the Board shall, within ninety days of the said attachment, obtain confirmation of the said attachment from the Special Court, established under section 26A, having jurisdiction and on such confirmation, such attachment shall continue during the pendency of the aforesaid proceedings and on conclusion of the said proceedings, the provisions of section 28A shall apply:

Provided further that only property, bank account or accounts or any transaction entered therein, so far as it relates to the proceeds actually involved in violation of any of the provisions of this Act, or the rules or the regulations made thereunder shall be allowed to be attached.

- (f) **direct any intermediary or any person associated** with the securities market in any manner not to dispose of or alienate an asset forming part of any transaction which is under investigation.

The amount disgorged, pursuant to a direction issued, under the SEBI Act or the Securities Contracts (Regulation) Act, 1956 or the Depositories Act, 1996, as the case may be-

- shall be credited to the Investor Protection and Education Fund (IPEF) established by the Board, and
- such amount shall be utilised by the Board in accordance with the regulations made under this Act.”.

Provided that the Board may take any of the measures specified in clause (d) or clause (e) or clause (f), in respect of any listed public company or a public company (not being intermediaries referred to in section 12) which intends to get its securities listed on any recognised stock exchange where the Board has reasonable grounds to believe that such company has been indulging in insider trading or fraudulent and unfair trade practices relating to securities market:

Provided further that the Board shall, either before or after passing such orders, give an opportunity of hearing to such intermediaries or persons concerned.

Penalty: The Board may, by an order, for reasons to be recorded in writing, levy penalty under sections 15A, 15B, 15C, 15D, 15E, 15EA, 15EB, 15F, 15G, 15H, 15HA and 15HB after holding an inquiry in the prescribed manner.

Consequences: The amount disgorged, pursuant to a direction issued, under various Acts i.e., section 11B of this Act or section 12A of the Securities Contracts (Regulation) Act, 1956 or section 19 of the Depositories Act, 1996 or under a settlement made under section 15JB or section 23JA of the Securities Contracts (Regulation) Act, 1956 or section 19-IA of the Depositories Act, 1996, as the case may be, shall be:

1. Credited to the Investor Protection and Education Fund established by the Board and
2. Such amount shall be utilized by the Board in accordance with the regulations made under this Act.

Example 1: The Securities and Exchange Board of India (SEBI) has received certain information and complaints which have led to it believe that DA Brokers Ltd, a registered Market Intermediary has violated multiple provisions of the SEBI regulations. In such a case, SEBI may, at any time by order in writing, direct any person (hereafter in this section referred to as the Investigating Authority) specified in the order to investigate the affairs of such intermediary or persons associated with the

securities market and to report thereon to the Board. Therefore, an order for an investigation into the affairs of the broker may be initiated.

Additional functions of SEBI under the Securities Contracts (Regulation) Act, 1956: The Securities Contracts (Regulation) Act, 1956 which was enacted to prevent undesirable transactions in securities and to regulate the business of securities had given certain powers to the Central Government, under the provisions of that Act. The functions of the Central Government under that Act have been granted to SEBI. These functions are:

- (a) **Power to call for periodical returns or direct enquiries to be made (Section 6 of SCRA):** SEBI will receive from every Recognised Stock Exchange such periodical returns relating to its affairs as may be prescribed by SCRA rules.

Description of Powers	Powers of SEBI
Power to inspect	It shall be open to SEBI to inspect at all reasonable times books of accounts and other documents to be maintained by the Stock Exchanges for periods not exceeding five years as may be prescribed in the public interest and in the interest of trade by the Central Government.
Power of SEBI to call for information/explanation relating to affairs of the stock exchange	It shall also be open to SEBI to call upon recognised stock exchanges or any member thereof to furnish in writing such information or explanation relating to the affairs of the Stock Exchange or of the member in relation to the stock exchange as may be required by SEBI in the interest of trade or in the public interest.
SEBI to appoint persons to make an inquiry	It shall also be open to SEBI to appoint, by order in writing, one or more persons to make an inquiry in the prescribed manner in relation to the affairs of the governing body of stock exchange or the affairs of any of the members of the stock exchange in relation to the stock exchange and submit a report of the result of such enquiry to SEBI within the time as, specified in the order. In the case of affairs of any of the members/ of a stock exchange, SEBI can direct the governing body of such stock exchange to make an inquiry and submit its report.
SEBI will bound the concerned persons to produce documents	Every director, manager, secretary or other officer of such stock exchange, every member of such stock

before himself /other enquiry officer	exchange and every constituent or agent of such member if it is a firm and every other person or body of persons having dealings with any of these persons whether directly or indirectly shall be bound to produce before SEBI or other enquiry officer, all books of accounts and other documents in his custody or power relating to the subject matter of the enquiry. This has to be done within the time specified and as may be required by the enquiry authority.

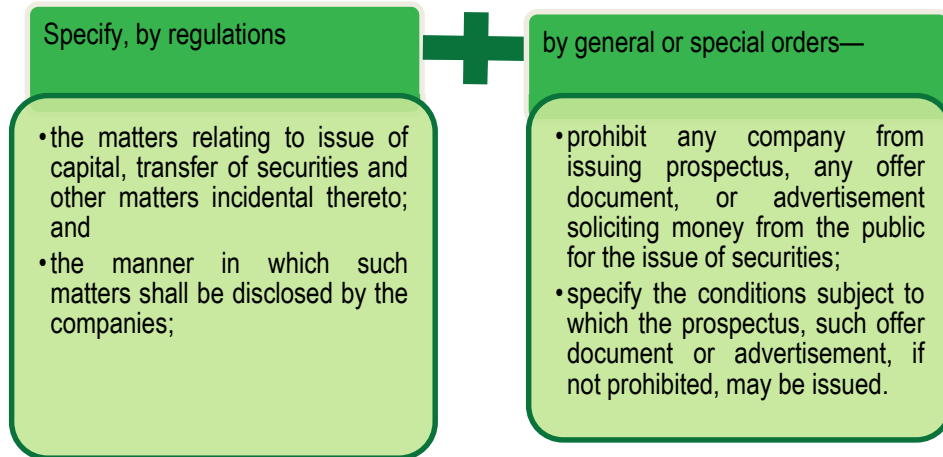
- (b) **Power to approve the bye-laws of stock exchanges:** Section 9 of SCRA provides that any recognised stock exchange may make bye-laws for the regulation and control of contracts with the previous approval of SEBI. Such bye-laws may provide for submission of periodical settlements carried out by clearing houses to SEBI or publication of such particulars by clearing houses subject to SEBI's directions. Such bye-laws have to be published for public comments and after approval by SEBI shall have to be published in the Gazette of India and also in the Official Gazette of the State unless SEBI, by written order with reasons dispense with the condition of previous publication.
- (c) **Power of SEBI to make or amend bye-laws of recognised stock exchanges (Section 10, SCRA):** SEBI may either on a request in writing received by it in this behalf from the governing body of a recognised stock exchange or on its own motion make bye-laws on matters specified in Section 9 of SCRA or amend any bye-laws made by such stock exchange. SEBI will have to be satisfied, after consultation with the governing body of the stock exchange, that it is necessary or expedient to make or amend the bye-laws and record its reasons also.
- (d) **Licensing of dealers in securities in certain areas (Section 17 SCRA):** SEBI has been empowered to grant a license to any person for the business of dealing in securities in any State or area to which Section 13 of SCRA has not been declared to apply. Section 13 of SCRA deals with contracts in notified areas to be illegal in certain circumstances.
- (e) **Public Issue and listing of securities referred to in section 2 (h) (ie) of SCRA:** As per section 17A, securities of the nature referred to in section 2 (h) (ie) shall be offered to the public or listed on any stock exchange unless the issuer fulfills eligibility criteria and complies with other requirements as may be specified by SEBI by regulations.
- (f) **Power to delegate:** Section 29A of SCRA provides that the Central Government may, by order published in the Official Gazette, direct that the powers exercisable by it under any provision of the SCRA shall, in relation to such matters and subject to such conditions, if any as may be specified in the order, be exercisable also by SEBI or the Reserve Bank of India.

More Powers for SEBI: Certain additional powers with regard to certain provisions under the Companies Act, 2013, related to issue and transfer of securities and non-payment of dividend, in the case of listed public companies intending to get their securities listed on any recognised stock exchange, shall be administered by SEBI.



5. BOARD TO REGULATE OR PROHIBIT ISSUE OF PROSPECTUS, OFFER DOCUMENT OR ADVERTISEMENT SOLICITING MONEY FOR ISSUE OF SECURITIES [SECTION 11A]

- (1) As per this section, the Board may, for the protection of investors,—



- (2) The Board may specify the requirements for listing and transfer of securities and other matters incidental thereto.



6. COLLECTIVE INVESTMENT SCHEME [SECTION 11AA]

Any scheme or arrangement which **satisfies the conditions** referred to in sub-section (2) or sub-section (2A) shall be a collective investment scheme.

Provided that any pooling of funds under any scheme or arrangement, which is not registered with the Board or is not covered under sub-section (3), involving a corpus amount of one hundred crore rupees or more shall be deemed to be a collective investment scheme.

Requisite conditions [Section 11AA(2)]: Any scheme or arrangement made or offered by any person under which, -

- the contributions, or payments made by the investors, by whatever name called, are **pooled and utilized** for the purposes of the scheme or arrangement;
- the contributions or payments are made to such scheme or arrangement by the investors with a view to receive **profits**, income, produce or property, whether movable or immovable, from such scheme or arrangement;
- the property, contribution or investment forming part of scheme or arrangement, whether

identifiable or not, is **managed on behalf of the investors**;

- (iv) the **investors do not have day-to-day control** over the management and operation of the scheme or arrangement.[Sub-section 2]

Section 11AA(2A): Any scheme or arrangement made or offered by any person satisfying the conditions as may be specified in accordance with the regulations made under this Act.

Exceptions [Section 11AA(3)]: Following scheme or arrangement shall not be a collective investment scheme-

- (i) made or offered by a **co-operative society** registered under the Co-operative Societies Act, 1912 or a society being a society registered or deemed to be registered under any law relating to co-operative societies for the time being in force in any State;
- (ii) under which **deposits are accepted by non-banking financial companies** as defined in clause (f) of section 45-I of the Reserve Bank of India Act, 1934;
- (iii) being a **contract of insurance** to which the Insurance Act, 1938 applies;
- (iv) providing for **any Scheme**, Pension Scheme or the Insurance Scheme framed **under the Employees' Provident Funds and Miscellaneous Provisions Act, 1952**;
- (v) under which **deposits are accepted under the Companies Act, 2013**
- (vi) under which **deposits are accepted by a company declared as a Nidhi or a mutual benefit society** under the Companies Act, 2013;
- (vii) falling within the meaning of **Chit business** as defined in clause (d) of section 2 of the Chit Fund Act, 1982;
- (viii) under which **contributions made are in the nature of subscription** to a mutual fund;
- (ix) such other **scheme or arrangement which the Central Government may**, in consultation with the Board, **notify**,



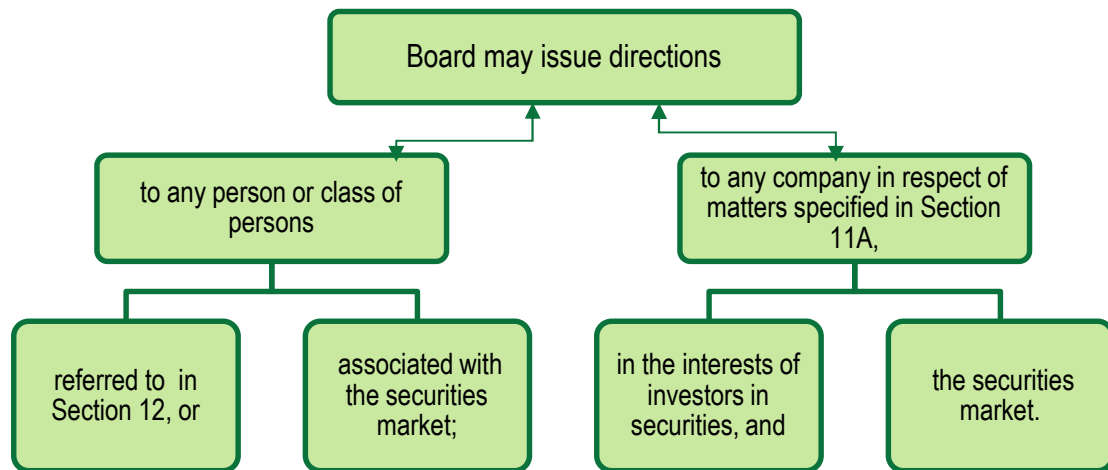
7. POWER TO ISSUE DIRECTIONS AND LEVY PENALTY [SECTION 11B]

Save as otherwise provided in Section 11, if after making or causing to be made an enquiry, the Board is satisfied that it is necessary:

in the interest of investors, or orderly development of securities market; or

to prevent the affairs of any intermediary or other persons referred to in Section 12 being conducted in a manner detrimental to interest of investors or securities market; or

to secure the proper management of any such intermediary or persons,



Levy of Penalty: The Board may, by an order, for reasons to be recorded in writing, levy penalty under sections 15A, 15B, 15C, 15D, 15E, 15EA, 15EB, 15F, 15G, 15H, 15HA and 15HB after holding an inquiry in the prescribed manner.

Explanation—For the removal of doubts, it is hereby declared that the **power to issue directions** under this section shall include and always be deemed to have been **included the power to direct** any person, who made profit or averted loss by indulging in any transaction or activity in contravention of the provisions of this Act or regulations made thereunder, **to disgorge an amount** equivalent to the wrongful gain made or loss averted by such contravention.



8. INVESTIGATION [SECTION 11C]

- (1) **Grounds for issue of an order of investigation:** Where the Board has reasonable ground to believe that—

- (a) the transactions in securities are being dealt with in a manner detrimental to the investors or the securities market; or
- (b) any intermediary or any person associated with the securities market has violated any of the provisions of this Act or the rules or the regulations made or directions issued by the Board there under.

It may, at any time by order in writing, direct any person (hereafter in this section referred to as the Investigating Authority) specified in the order to investigate the affairs of such intermediary or persons associated with the securities market and to report thereon to the Board.

- (2) **Furnishing of relevant documents to the investigating authority:** It shall be the duty of-
- every manager, managing director, officer and other employee of the company and every intermediary referred to in section 12, or
 - every person associated with the securities market,

to **preserve**, and to **produce** to the Investigating Authority or any person authorised by it in this behalf, all the books, registers, other documents and record of, or relating to, the company or, as the case may be, of or relating to, the intermediary or such person, which are in their custody or power.

- (3) **Period of custody:** The Investigating Authority may keep in its custody any books, registers, other documents and record produced for **six months** and thereafter shall return the same to any intermediary or any person associated with securities market by whom or on whose behalf the books, registers, other documents and record are produced:

The Investigating Authority may call for any book, register, other document and record if they are needed again.

If the person on whose behalf the books, registers, other documents and record are produced requires certified copies of the books, registers, other documents and record produced before the Investigating Authority, it shall give certified copies of such books, registers, other documents and record to such person or on whose behalf the books, registers, other documents and record were produced.

- (4) **Examination on oath:** Any person, directed to make an investigation, may examine on oath, any manager, managing director, officer and other employee of any intermediary or any person associated with securities market in any manner, in relation to the affairs of his business and may administer an oath accordingly and for that purpose may require any of those persons to appear before it personally.

- (5) **On failure:** If any person fails without reasonable cause or refuses—

Failure in compliance	Punishment
(a) to produce to the Investigating Authority or any person authorised by it in this behalf any book, register, other document and record which is his duty to produce; or (b) to furnish any information which is his duty to furnish; or (c) to appear before the Investigating Authority personally or to answer any question which is put to him by the Investigating Authority in pursuance of that sub-section; or (d) to sign the notes of any examination,	Person shall be punishable with- • imprisonment for a term which may extend to one year, or • with fine, which may extend to one crore rupees, or • with both, and • also with a further fine which may extend to five lakh rupees for every day after the first during which the failure or refusal continues.

- (6) **Notes of examination to be used as examination:** Notes of any examination shall be taken down in writing and shall be read over to, or by, and signed by, the person examined, and may thereafter be used in evidence against him.
- (7) **Impounding of documents :**Where in the course of investigation, the Investigating Authority has reasonable ground to believe that the books, registers, other documents and record of, or relating to, any intermediary or any person associated with securities market in any manner, may be destroyed, mutilated, altered, falsified or secreted, the Investigating Authority may make an application to the Magistrate or Judge of such designated court in Mumbai, as may be notified by the Central Government for an order for the seizure of such books, registers, other documents and record.
- (8) **Demand of services of other officers:** The authorized officer may requisition the services of any police officer or any officer of the Central Government, or of both, to assist him for all or any of the purposes as specified above with respect to impounding of documents and it shall be the duty of every such officer to comply with such requisition.
- (9) **Order of court:** After considering the application and hearing the Investigating Authority, if necessary, the Magistrate or Judge of the Designated Court may, by order, authorise the Investigating Authority –

to enter, with such assistance, as may be required, the place or places where such books, registers, other documents and record are kept;

to search that place or those places in the manner specified in the order; and

to seize books, registers, other documents and record, it considers necessary for the purposes of the investigation:

Exemptions: Provided that the Magistrate or Judge of the Designated Court shall not authorise seizure of books, registers, other documents and record, of any listed public company or a public company (not being the intermediaries specified under section 12) which intends to get its securities listed on any recognised stock exchange unless such company indulges in insider trading or market manipulation.

- (10) **Impounded documents will remain in the custody of investigating authority:** The Investigating Authority shall keep in its custody the books, registers, other documents and record seized under this section for such **period not later than the conclusion of the investigation** as it considers necessary and **thereafter shall return** the same to the company or the other body corporate, or, as the case may be, to the managing director or the manager or any other person, from whose custody or power they were seized **and inform** the Magistrate or Judge of the Designated Court of such return:

Provided that the Investigating Authority may, before returning such books, registers, other documents and record as aforesaid, place identification marks on them or any part thereof.

- (11) Every search or seizure made under this section shall be carried out in accordance with the provisions of the Code of Criminal Procedure, 1973 (2 of 1974) relating to searches or seizures made under that Code.



9. CEASE AND DESIST PROCEEDINGS [SECTION 11D]

If the Board finds, after causing an inquiry to be made, that any person has violated, or is likely to violate, any provisions of this Act, or any rules or regulations made thereunder, it may pass an order requiring such person to cease and desist from committing or causing such violation:

Provided that the Board shall not pass such order in respect of any listed public company or a public company (other than the intermediaries specified under section 12) which intends to get its securities listed on any recognised stock exchange unless the Board has reasonable grounds to believe that such company has indulged in insider trading or market manipulation.”



10. REGISTRATION CERTIFICATE [SECTION 12]

Provision related to	Provides
Persons who are authorized to buy, sell or deal in securities	Stock broker, sub-broker, share transfer agent, banker to an issue, trustee of trust deed, registrar to an issue, merchant banker, underwriter, portfolio manager, investment adviser and such other intermediary who may be associated with securities market shall buy, sell or deal in securities in accordance with, the conditions of a certificate of registration obtained from the Board in accordance with the regulations made under this Act
Board may by notification specify the persons who shall buy or sell or deal in securities	Depository, participant, custodian of securities, foreign institutional investor, credit rating agency, or any other intermediary associated with the securities market as the Board may by notification in this behalf specify, shall buy or sell or deal in securities in accordance with the conditions of a certificate of registration obtained from the Board in accordance with the regulations made under this Act;
Person who shall sponsor or cause to be sponsored or carry on or caused to be carried on any venture capital funds and collective investment scheme including mutual funds	Shall be, who obtains certificate of registration from the Board in accordance with the regulations.
Person who shall sponsor or cause to be sponsored or carry on or caused to be carried on the activity of an alternative investment fund or a business trust as defined in clause (13A) of section 2 of the Income-tax Act, 1961	Shall be, who obtains certificate of registration from the Board in accordance with the regulations.

Manner of application for registration: Every application for registration shall be in such manner and on payment of such fees as may be determined by regulations.

Suspension /cancellation of a certificate of registration: The Board may, by order, suspend or cancel a certificate of registration in such manner as may be determined by regulations; Provided that no order under this sub-section shall be made unless the person concerned has been -given a reasonable opportunity of being heard.



11. PROHIBITION OF MANIPULATIVE AND DECEPTIVE DEVICES, INSIDER TRADING AND SUBSTANTIAL ACQUISITION OF SECURITIES OR CONTROL [SECTION 12A]

Prohibition on person	From performing following activities
No person shall directly or indirectly	use or employ in connection with the issue, purchase or sale of any securities listed or proposed to be listed on a recognized stock exchange, - any manipulative or deceptive device or - contrivance in contravention of the provisions of this Act or the rules or the regulations made thereunder;
	employ any device, scheme or artifice to defraud in connection with issue or dealing in securities which are listed or proposed to be listed on a recognised stock exchange;
	engage in any act, practice, course of business which operates or would operate as fraud or deceit upon any person, in connection with the issue, dealing in securities which are listed or proposed to be listed on a recognised stock exchange, in contravention of the provisions of this Act or the rules or the regulations made thereunder;
	engage in insider trading;
	deal in securities while in possession of material or non-public information or communicate such material or non-public information to any other person, in a manner which is in contravention of the provisions of this Act or the rules or the regulations made thereunder;
	acquire control of any company or securities more than the percentage of equity share capital of a company whose securities are listed or proposed to be listed on a recognised stock exchange in contravention of the regulations made under this Act.



12. FINANCE, ACCOUNTS AND AUDIT

Grants by the Central Government [Section 13]

The Central Government may, after due appropriation made by Parliament by law in this behalf, make to the Board grants of such sums of money as that Government may think fit for being utilized for the purposes of this Act.

Fund [Section 14]

- (1) There shall be constituted a Fund to be called the Securities and Exchange Board of India General Fund and there shall be credited thereto-
 - all grants, fees and charges received by the Board under this Act;
 - all sums received by the Board from such other sources as may be decided upon by the Central Government.
- (2) The Fund shall be applied for meeting—
 - the salaries, allowances and other remuneration of the members, officers and other employees of the Board;
 - the expenses of the Board in the discharge of its functions under section 11;
 - the expenses on objects and for purposes authorised by this Act.

Accounts and audit [Section 15]

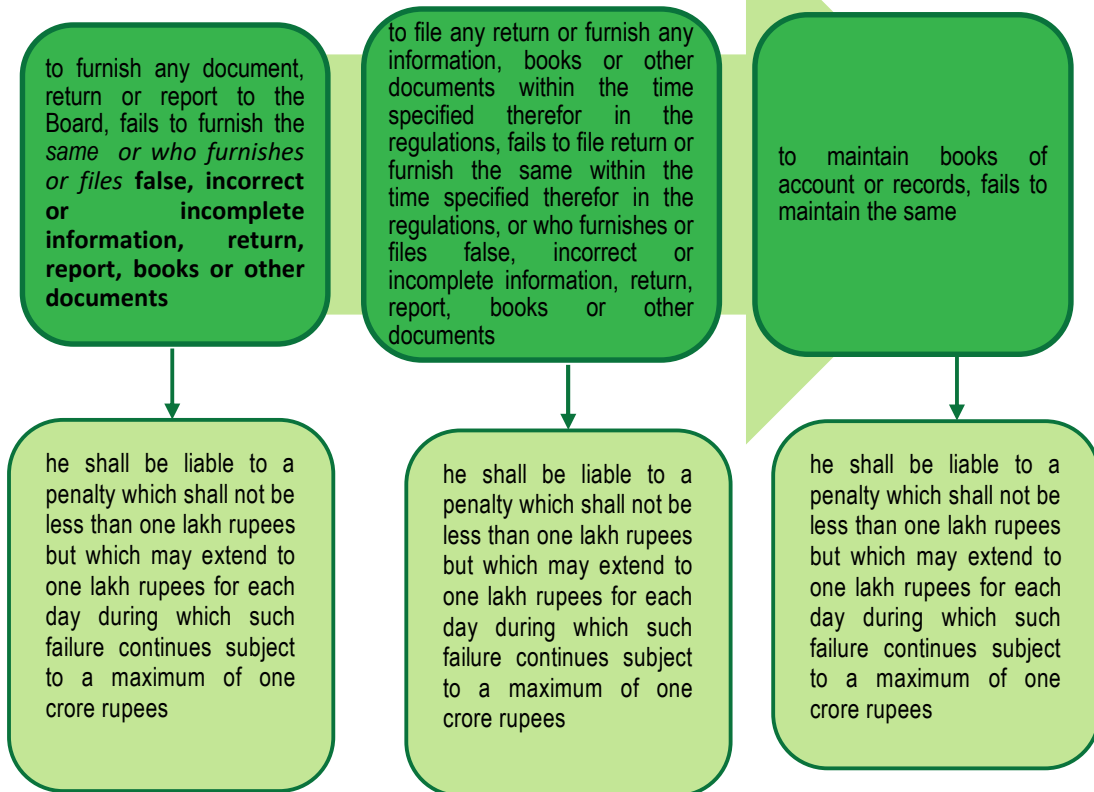
- (1) **Preparation of annual financial statement of Board in consultation with CAG of India:** The Board shall maintain proper accounts and other relevant records and prepare an annual statement of accounts in such form as may be prescribed by the Central Government in consultation with the Comptroller and Auditor-General of India.
- (2) **Audit of accounts of Board:** The accounts of the Board shall be audited by the Comptroller and Auditor-General of India at such intervals as may be specified by him and any expenditure incurred in connection with such audit shall be payable by the Board to the Comptroller and Auditor-General of India.
- (3) **Right and Privileges:** The Comptroller and Auditor-General of India and any other person appointed by him in connection with the audit of the accounts of the Board shall have the same rights and privileges and authority in connection with such audit as the Comptroller and Auditor-General generally has in connection with the audit of the Government accounts and, in particular, shall have the right to demand the production of books, accounts, connected vouchers and other documents and papers and to inspect any of the offices of the Board.
- (4) **Certified Accounts and Audit reports to be forwarded to the Central Government:** The accounts of the Board as certified by the Comptroller and Auditor-General of India or any other person appointed by him in this behalf together with the audit report thereon shall be forwarded annually to the Central Government and that Government shall cause the same to be laid before each House of Parliament.



13. PENALTIES AND ADJUDICATION

Penalty for failure to furnish information, return, etc. [Section 15A]

If any person, who is required under this Act or any rules or regulations made thereunder,—



Penalty for failure by any person to enter into agreement with clients [Section 15B]

If any person, who is registered as an intermediary and is required under this Act or any rules or regulations made thereunder to enter into an agreement with his client, fails to enter into such agreement,

- he shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one lakh rupees for each day during which such failure continues subject to a maximum of one crore rupees.

Penalty for failure to redress investors' grievances [Section 15C]

If any listed company or any person who is registered as an intermediary, after having been called upon by the Board in writing, to redress the grievances of investors, fails to redress such grievances within the time specified by the Board,

- such company or intermediary shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one lakh rupees for each day during which such failure continues subject to a maximum of one crore rupees.

Penalty for certain defaults in case of mutual funds [Section 15D]

Person liable	For defaults	Punishments levied
If any person, who is—	required under this Act or any rules or regulations made thereunder to obtain a certificate of registration from the Board for sponsoring or carrying on any collective investment scheme), including mutual funds, sponsors or carries on any collective investment scheme, including mutual funds, without obtaining such certificate of registration	he shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one lakh rupees for each day during which he sponsors or carries on any such collective investment scheme including mutual funds subject to a maximum of one crore rupees;
	registered with the Board as a collective investment scheme, including mutual funds, for sponsoring or carrying on any investment scheme, fails to comply with the terms and conditions of certificate of registration	he shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one lakh rupees for each day during which such failure continues subject to a maximum of one crore rupees;
	registered with the Board as a collective investment scheme, including mutual funds, fails to make an application for listing of its schemes as provided for in the regulations governing such listing	he shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one lakh rupees for each day during which such failure continues subject to a maximum of one crore rupees;
	registered as a collective investment scheme, including	he shall be liable to a penalty which shall not be less than one lakh

	mutual funds, fails to dispatch unit certificates of any scheme in the manner provided in the regulation governing such dispatch	rupees but which may extend to one lakh rupees for each day during which such failure continues subject to a maximum of one crore rupees;
	registered as a collective investment scheme, including mutual funds, fails to refund the application monies paid by the investors within the period specified in the regulations	he shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one lakh rupees for each day during which such failure continues subject to a maximum of one crore rupees
	registered as a collective investment scheme, including mutual funds, fails to invest money collected by such collective investment schemes in the manner or within the period specified in the regulations	he shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one lakh rupees for each day during which such failure continues subject to a maximum of one crore rupees.

Penalty for failure to observe rules and regulations by an asset management company [Section 15E]

Where any asset management company of a mutual fund registered under this Act, fails to comply with any of the regulations providing for restrictions on the activities of the asset management companies,

- such asset management company shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one lakh rupees for each day during which such failure continues subject to a maximum of one crore rupees

Penalty for default in case of alternative investment funds, infrastructure investment trusts and real estate investment trusts [Section 15 EA]

Where any person fails to comply with the regulations made by the Board in respect of:

- ✓ alternative investment funds,
- ✓ infrastructure investment trusts, and
- ✓ real estate investment trusts or
- ✓ fails to comply with the directions issued by the Board,
- such person shall be liable to penalty which shall not be less than one lakh rupees but which may extend to one lakh rupees for each day during which such failure continues subject to a

maximum of one crore rupees or three times the amount of gains made out of such failure, whichever is higher.

Penalty for default in case of investment adviser and research analyst [Section 15EB]

Where an investment adviser or a research analyst fails to comply with the regulations made by the Board or directions issued by the Board,

- such investment adviser or research analyst shall be liable to penalty which shall not be less than one lakh rupees but which may extend to one lakh rupees for each day during which such failure continues subject to a maximum of one crore rupees.

Penalty for default in case of stock brokers [Section 15 F]

Person, registered as a stock broker	fails to issue	contract notes in the form and manner specified by the stock exchange of which such broker is a member,	he shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one crore rupees for which the contract note was required to be issued by that broker
	fails to deliver	any security or fails to make payment of the amount due to the investor in the manner within the period specified in the regulations	he shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one lakh rupees for each day during which such failure continues subject to a maximum of one crore rupees
	charges	an amount of brokerage which is in excess of the brokerage specified in the regulations	he shall be liable for penalty which shall not be less than one lakh rupees but which may extend to five times the amount of brokerage charged in excess of the specified brokerage, whichever is higher

Penalty for insider trading [Section 15G]

Any insider shall be liable to a penalty which shall not be less than ten lakh rupees but which may extend to twenty-five crore rupees / three times the amount of profits made out of insider trading, whichever is higher, who-

either on his own behalf or on behalf of any other person

communicates any unpublished price-sensitive information to any person, with or without his request for such information

counsels, or procures for any other person to deal in any securities of any body corporate on the basis of unpublished price-sensitive information

deals in securities of a body corporate listed on any stock exchange on the basis of any unpublished price-sensitive information; or

except as required in the ordinary course of business or under any law, or

Penalty for non-disclosure of acquisition of shares and takeovers [Section 15 H]

If any person, who is required under this Act or any rules or regulations made thereunder, fails to,—

disclose the aggregate of his shareholding in the body corporate before he acquires any shares of that body corporate; or

make a public announcement to acquire shares at a minimum price; or

make a public offer by sending letter of offer to the shareholders of the concerned company; or

make payment of consideration to the shareholders who sold their shares pursuant to letter of offer,

he shall be liable to a penalty which shall not be less than ten lakh rupees but which may extend to twenty-five crore rupees or three times the amount of profits made out of such failure, whichever is higher.

Penalty for fraudulent and unfair trade practices [Section 15HA]

If any person indulges in fraudulent and unfair trade practices relating to securities, he shall be liable to a penalty which shall –

- not be less than five lakh rupees but
 - which may extend to twenty-five crore rupees or three times the amount of profits made out of such practices,.
- { Whichever is higher }

Penalty for alteration destruction, etc., of records and failure to protect the electronic database of Board [15HAA]

Any person, who—

- (a) knowingly alters, destroys, mutilates, conceals, falsifies, or makes a false entry in any information, record, document (including electronic records), which is required under this Act or any rules or regulations made thereunder, so as to impede, obstruct, or influence the investigation, inquiry, audit, inspection or proper administration of any matter within the jurisdiction of the Board.

Explanation.— For the purposes of this clause, a person shall be deemed to have altered, concealed or destroyed such information, record or document, in case he knowingly fails to immediately report the matter to the Board or fails to preserve the same till such information continues to be relevant to any investigation, inquiry, audit, inspection or proceeding, which may be initiated by the Board and conclusion thereof;

- (b) without being authorised to do so, access or tries to access, or denies of access or modifies access parameters, to the regulatory data in the database;
- (c) without being authorised to do so, downloads, extracts, copies, or reproduces in any form the regulatory data maintained in the system database;
- (d) knowingly introduces any computer virus or other computer contaminant into the system database and brings out a trading halt;
- (e) without authorisation disrupts the functioning of system database;
- (f) knowingly damages, destroys, deletes, alters, diminishes in value or utility, or affects by any means, the regulatory data in the system database; or
- (g) knowingly provides any assistance to or causes any other person to do any of the acts specified in clauses (a) to (f),

shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to ten crore rupees or three times the amount of profits made out of such act, whichever is higher.

Explanation.—In this section, the expressions "computer contaminant", "computer virus" and "damage" shall have the meanings respectively assigned to them under section 43 of the Information Technology Act, 2000.

Penalty for contravention where no separate penalty has been provided [Section 15HB]

Whoever fails to comply with any provision of this Act, the rules or the regulations made or directions issued by the Board thereunder for which no separate penalty has been provided, shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one crore rupees.

Summary of Section 15A to 15HB

Sec	Kind of Failure:	Penalty
15A	a. Fails to furnish any document, return or report to the Board or furnishes or files false, incorrect or incomplete information, return, report, books or other documents. b. Fails to file any return or furnish any information, books or other documents within time specified or who furnishes or files false, incorrect, or incomplete information, return, report, books or other documents. c. Fails to maintain books of account or records.	₹ 1 lakh + ₹ 1 lakh / day up to ₹ 1 Crore.
15B	If any person registered u/s 12 is required by the Act to enter into an agreement with his client , fails to enter into such agreement	₹ 1 lakh + ₹ 1 lakh / day up to ₹ 1 Crore.
15C	If any listed company or any person who is registered u/s 12, after having been called upon by the Board, to redress the grievances of investors , fails to redress such grievances within the time specified by the Board, such company or intermediary	₹ 1 lakh + ₹ 1 lakh / day up to ₹ 1 Crore.
15D	If any person, who is: a. required u/s 12 to obtain a CoR for sponsoring or carrying on any CIS, including MF, sponsors or carries on any such activity without obtaining such CoR b. registered as a CIS u/s 12 but fails to - comply with the T&C of CoR - to make an application for listing of its schemes as provided for in the regulations governing such listing dispatch unit certificates of any scheme in the manner provided in the regulation governing such dispatch refund the application monies paid by the investors within the period specified in the regulations	₹ 1 lakh + ₹ 1 lakh / day up to ₹ 1 Crore

	• Invest money collected by such CIS as per regulations	
15E	Where any AMC of a MF registered under this Act, fails to comply with any of the regulations providing for restrictions on the activities of the AMC, such AMC:	₹ 1 lakh + ₹ 1 lakh / day up to ₹ 1 Crore
15EA	Where any person fails to comply with the regulations in respect of, • alternative investment funds, • infrastructure investment trusts, and • real estate investment trusts or or fails to comply with the directions issued by the Board, shall be liable to	₹ 1 lakh + ₹ 1 lakh / day up to (Higher of ₹ 1 Crore or 3 times of the gain made out of such failure)
15EB	Where an investment adviser or a research analyst fails to comply with the regulations or directions issued by the Board, such investment adviser or research analyst	₹ 1 lakh + ₹ 1 lakh / day up to ₹ 1 Crore
15F	If any person, who is registered as a stockbroker under this Act: (a) fails to issue contract notes in the form and manner specified by the stock exchange of which such broker is a member	₹ 1 lakh up to ₹ 1 Crore
15F	(b) fails to deliver any security or fails to make payment of the amount due to the investor as per the regulations	₹ 1 lakh + ₹ 1 lakh / day up to ₹ 1 Crore
15F	(c) charges an amount of brokerage which is in excess of the brokerage specified in the regulations	₹ 1 lakh up to 5 times the amount of brokerage charged in excess of the specified brokerage
15G	If any insider who: a. either on his own behalf or on behalf of any other person, deals in securities of a body corporate listed on any stock exchange on the basis of any unpublished price-sensitive information; or b. communicates any unpublished price-sensitive information to any person, with or without his request for such information except as required in the ordinary course of business or under any law; or c. counsels, or procures for any other person to deal in any securities of any body corporate on the basis of unpublished price-sensitive information	₹ 10 lakhs up to (Higher of ₹ 25 Crores or 3X amount of profit made)

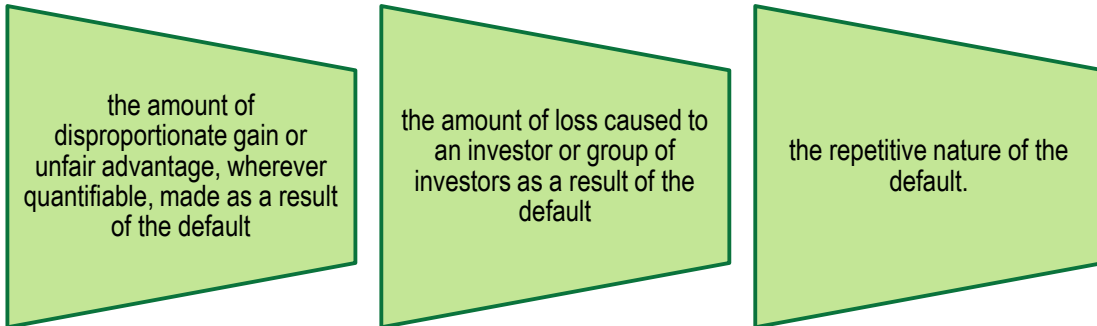
15H	If any person, who is required under this Act/rules/regulations, fails to: disclose the aggregate of his shareholding in the body corporate before he acquires any shares of that body corporate; or - make a public announcement to acquire shares at a minimum price; or - make a public offer by sending letter of offer to the shareholders of the concerned company; or - make payment of consideration to the shareholders who sold their shares pursuant to letter of offer	₹ 10 lakhs up to (Higher of ₹ 25 Crores or 3X amount of profit made)
15HA	If any person indulges in fraudulent and unfair trade practices relating to securities	₹ 5 lakhs up to (Higher of ₹ 25 Crores or 3X amount of profit made)
15HAA	Any person, who: - knowingly DAMFS any information, record, document (including e-records) required to be maintained as per the Act, so as to impede, obstruct, or influence the Ill, Audit, or proper administration of any matter within the jurisdiction of the Board. - without being authorised to do so, access or tries to access, or denies or modifies access parameters, to the regulatory data in the database; - without being authorised to do so, downloads, extracts, copies, or reproduces in any form the regulatory data maintained in the system database; - knowingly introduces any computer virus or other computer contaminant into the system database and brings out a trading halt; - without authorisation disrupts the functioning of system database; - knowingly damages, destroys, deletes, alters, diminishes in value or utility, or affects by any means, the regulatory data in the system database; or - knowingly provides any assistance to or causes any other person to do any of the acts specified in clauses (a) to (f)	₹ 1 lakh up to (Higher of ₹ 10 Crores or 3X amount of profit made)
15HB	Person fails to comply with any provision of this Act/Rules/Regulations/directions issued by the Board for which no separate penalty has been provided	₹ 1 lakh up to ₹ 1 Crore

Power to adjudicate [Section 15-I]

On the matters related to	Power to adjudicate
For the purpose of adjudging under sections 15A, 15B, 15C, 15D, 15E, 15EA, 15EB, 15F, 15G, 15H, 15HA and 15HB	Board may appoint any officer not below the rank of a Division Chief to be an adjudicating officer for holding an inquiry in the prescribed manner after giving any person concerned a reasonable opportunity of being heard for the purpose of imposing any penalty.
On holding of an inquiry	The adjudicating officer shall have power to: • summon and enforce the attendance of any person acquainted with the facts and circumstances of the case to give evidence or • to produce any document which in the opinion of the adjudicating officer, may be useful for or relevant to the subject-matter of the inquiry and • if, on such inquiry, he is satisfied that the person has failed to comply with the provisions of any of the sections specified in subsection (1), he may impose such penalty as he thinks fit in accordance with the provisions of any of those sections.
Order passed by adjudicating officer is not justified	The Board may call for and examine the record of any proceedings and if it considers that the order passed by the adjudicating officer is erroneous to the extent it is not in the interests of the securities market, it may, after making or causing to be made such inquiry as it deems necessary, pass an order enhancing the quantum of penalty, if the circumstances of the case so justify: Provided that no such order shall be passed unless the person concerned has been given an opportunity of being heard in the matter: Limitation period: Provided further that nothing contained in this sub-section shall be applicable after an expiry of a period of three months from the date of the order passed by the adjudicating officer or disposal of the appeal under section 15T, whichever is earlier.

Factors to be taken into account while adjudging quantum of penalty [Section 15J]

While adjudging quantum of penalty under section 15-I or section 11 or section 11B, the Board or the adjudicating officer, shall have due regard to the following factors, namely:—



It is clarified here that the power to adjudge the quantum of penalty under sections 15A to 15E, clauses (b) and (c) of sections 15F, 15G, 15H and 15HA shall be and shall always be deemed to have been exercised under the provisions of this section.

Crediting sums realised by way of penalties to Consolidated Fund of India [Section 15JA]

All sums realised by way of penalties under this Act shall be credited to the Consolidated Fund of India.

Settlement of administrative and civil proceedings [Section 15 JB]

- (1) **Filing of an application:** Any person, against whom any proceedings have been initiated or may be initiated under section 11, section 11B, section 11D, sub-section (3) of section 12 or section 15-I, may file an application in writing to the Board proposing for settlement of the proceedings initiated or to be initiated for the alleged defaults.
- (2) **Board may consider for settlement of defaults:** The Board may, after taking into consideration the nature, gravity and impact of defaults, agree to the proposal for settlement, on payment of such sum by the defaulter or on such other terms as may be determined by the Board in accordance with the regulations made under this Act.
- (3) **Mode of settlement proceedings:** The settlement proceedings under this section shall be conducted in accordance with the procedure specified in the regulations made under this Act.
- (4) **Order not appealable:** No appeal shall lie under section 15T against any order passed by the Board or adjudicating officer, as the case may be, under this section.
- (5) **Settlement amount to be credited to consolidated fund of India:** All settlement amounts, excluding the disgorgement amount and legal costs, realised under this Act shall be credited to the Consolidated Fund of India.



14. ESTABLISHMENT, JURISDICTION, AUTHORITY AND PROCEDURE OF SECURITIES APPELLATE TRIBUNAL (SAT)

Establishment of Securities Appellate Tribunals [Section 15K]

- (1) The Central Government shall, by notification, **establish a Tribunal** to be known as the Securities Appellate Tribunal to exercise the jurisdiction, powers and authority conferred on it by or under this Act or any other law for the time being in force.
- (2) The Central Government shall also specify in the notification referred to in sub-section (1), **the matters and places in relation to which the Securities Appellate Tribunal may exercise jurisdiction.**

Composition of Securities Appellate Tribunal [Section 15L]

- (1) **Composition:** The Securities Appellate Tribunal shall consist of a Presiding Officer and such number of Judicial Members and Technical Members as the Central Government may determine, by notification, to exercise the powers and discharge the functions conferred on the Securities Appellate Tribunal under this Act or any other law for the time being in force.
- (2) Subject to the provisions of this Act,—
 - (a) the jurisdiction of the Securities Appellate Tribunal may be exercised by Benches thereof;
 - (b) a Bench may be constituted by the Presiding Officer of the Securities Appellate Tribunal with two or more Judicial or Technical Members as he may deem fit:
Provided that every Bench constituted shall include at least one Judicial Member and one Technical Member;
 - (c) the Benches of the Securities Appellate Tribunal shall ordinarily sit at Mumbai and may also sit at such other places as the Central Government may, in consultation with the Presiding Officer, notify.
- (3) **Transfer of members:** The Presiding Officer may transfer a Judicial Member or a Technical Member of the Securities Appellate Tribunal from one Bench to another Bench.

Qualification for appointment as Presiding Officer or Member of Securities Appellate Tribunal [Section 15M]

A person shall not be qualified for appointment as the Presiding Officer or a Judicial Member or a Technical Member of the Securities Appellate Tribunal, unless he—

- (a) is, or has been, a Judge of the Supreme Court or a Chief Justice of a High Court or a Judge of High Court for at least seven years, in the case of the Presiding Officer; and

- (b) is, or has been, a Judge of High Court for at least five years, in the case of a Judicial Member; or
- (c) in the case of a Technical Member—
 - (i) is, or has been, a Secretary or an Additional Secretary in the Ministry or Department of the Central Government or any equivalent post in the Central Government or a State Government; or
 - (ii) is a person of proven ability, integrity and standing having special knowledge and professional experience, of not less than fifteen years, in financial sector including securities market or pension funds or commodity derivatives or insurance.

Appointment of judicial member [Section 15MA]

The Presiding Officer and Judicial Members of the Securities Appellate Tribunal shall be appointed by the Central Government in consultation with the Chief Justice of India or his nominee.

Appointment of technical member [Section 15MB]

- (1) The Technical Members of the Securities Appellate Tribunal shall be appointed by the Central Government on the recommendation of a Search-cum-Selection Committee consisting of the following, namely:—
 - (a) Presiding Officer, Securities Appellate Tribunal—Chairperson;
 - (b) Secretary, Department of Economic Affairs—Member;
 - (c) Secretary, Department of Financial Services—Member; and
 - (d) Secretary, Legislative Department or Secretary, Department of Legal Affairs—Member.
- (2) The Secretary, Department of Economic Affairs shall be the Convener of the Search-cum-Selection Committee.
- (3) The Search-cum-Selection Committee shall determine its procedure for recommending the names of persons to be appointed under sub-section (1).

Validity of appointment of Presiding officer and members of SAT [Section 15MC]

- (1) No appointment of the Presiding Officer, a Judicial Member or a Technical Member of the Securities Appellate Tribunal shall be invalid merely by reason of any vacancy or any defect in the constitution of the Search cum- Selection Committee.
- (2) **Disqualification of members:** A member or part time member of the Board or the Insurance Regulatory and Development Authority or the Pension Fund Regulatory and Development Authority, or any person at senior management level equivalent to the Executive Director in the Board or in such Authorities, shall not be appointed as Presiding Officer or Member of the Securities Appellate Tribunal, during his service or tenure as such with the Board or with such

Authorities, as the case may be, or within two years from the date on which he ceases to hold office as such in the Board or in such Authorities.

- (3) **Effect of holding of office by officer or members on commencement of Finance Act, 2017:** The Presiding Officer or such other member of the Securities Appellate Tribunal, holding office on the date of commencement of Part VIII of Chapter VI of the Finance Act, 2017 shall continue to hold office for such term as he was appointed and the other provisions of this Act shall apply to such Presiding Officer or such other member, as if Part VIII of Chapter VI of the Finance Act, 2017 had not been enacted.

Tenure of office of Presiding Officer and other Members of Securities Appellate Tribunal [Section 15N]

The Presiding Officer or every Judicial or Technical Member of the Securities Appellate Tribunal shall hold office for a **term of five years** from the date on which he enters upon his office, and shall be **eligible for reappointment for another term** of maximum five years:

Provided that no Presiding Officer or the Judicial or Technical Member shall hold office after he has attained the age of **seventy years**.

Salary and allowances and other terms and conditions of service of Presiding Officers [Section 15-O]

The salary and allowances payable to and the other terms and conditions of service including pension, gratuity and other retirement benefits of the Presiding Officer and other Members of a Securities Appellate Tribunal shall be such **as may be prescribed**.

Provided that neither the salary and allowances nor the other terms and conditions of service of the Presiding Officer and other Members of a Securities Appellate Tribunal shall be varied to their disadvantage after appointment.

Filling up of vacancies [Section 15P]

If, for reason other than temporary absence, any vacancy occurs in the office of the Presiding Officer or any other Member of a Securities Appellate Tribunal-

- then the Central Government shall appoint another person in accordance with the provisions of this Act to fill the vacancy, and
- the proceedings may be continued before the Securities Appellate Tribunal from the stage at which the vacancy is filled.

In the event of occurrence of any vacancy in the office of the **Presiding Officer** of the Securities Appellate Tribunal by reason of his death, resignation or otherwise, the senior-most Judicial Member of the Securities Appellate Tribunal shall act as the Presiding Officer until the date on which a new Presiding Officer is appointed in accordance with the provisions of this Act. **[Section 15PA]**

Resignation and removal [section 15Q]

- (1) **Resignation by notice in writing:** The Presiding Officer or any other Member of a Securities Appellate Tribunal may, by notice in writing under his hand addressed to the Central Government, resign his office.

Provided that the Presiding Officer or any other Member shall, unless he is permitted by the Central Government to relinquish his office sooner, continue to hold office-

- until the expiry of three months from the date of receipt of such notice or
 - until a person duly appointed as his successor enters upon his office or
 - until the expiry of his term of office,
- (Whichever is the earliest)

- (2) **Removal of Presiding officer/Judicial member/Technical member:** The Central Government may, after an inquiry made by the Judge of the Supreme Court, remove the Presiding Officer or Judicial Member or Technical Member of the Securities Appellate Tribunal, if he—

- (a) is, or at any time has been adjudged as an **insolvent**;
- (b) has become physically or mentally **incapable** of acting as the Presiding Officer, Judicial or Technical Member;
- (c) has been **convicted** of any offence which, in the opinion of the Central Government, involves moral turpitude;
- (d) has, in the opinion of the Central Government, so **abused his position** as to render his continuation in office detrimental to the public interest; or
- (e) has **acquired** such financial **interest** or other interest as is likely to affect prejudicially his functions as the Presiding Officer or Judicial or Technical Member:

Provided that he shall not be removed from office under clauses (d) and (e), unless he has been given a **reasonable opportunity of being heard** in the matter.

- (3) **Central Government authorized to regulate the procedure of investigation:** The Central Government may, by rules, regulate the procedure for the investigation of misbehavior or incapacity of the Presiding Officer or any other Member.

Appointment, qualification and the other terms and conditions of service of the Presiding Officer and other Members of the Appellate Tribunal to be governed by Finance Act, 2017 [Section 15QA]

- (i) **Where the qualification, appointment etc. is after the commencement of Finance Act, 2017:** Notwithstanding anything contained in this Act, the qualifications, appointment, term of office, salaries and allowances, resignation, removal and the other terms and conditions of service of the Presiding Officer and other Members of the Appellate Tribunal appointed after

the commencement of Part XIV of Chapter VI of the Finance Act, 2017, shall be governed by the provisions of section 184 of that Act.

- (ii) **Where the qualification, appointment etc. is before the commencement of Finance Act, 2017:** Provided that the Presiding Officer and Member appointed before the commencement of Part XIV of Chapter VI of the Finance Act, 2017, shall continue to be governed by the provisions of this Act and the rules made thereunder as if the provisions of section 184 of the Finance Act, 2017 had not come into force.

Orders constituting Appellate Tribunal to be final and not to invalidate its proceedings [Section 15R]

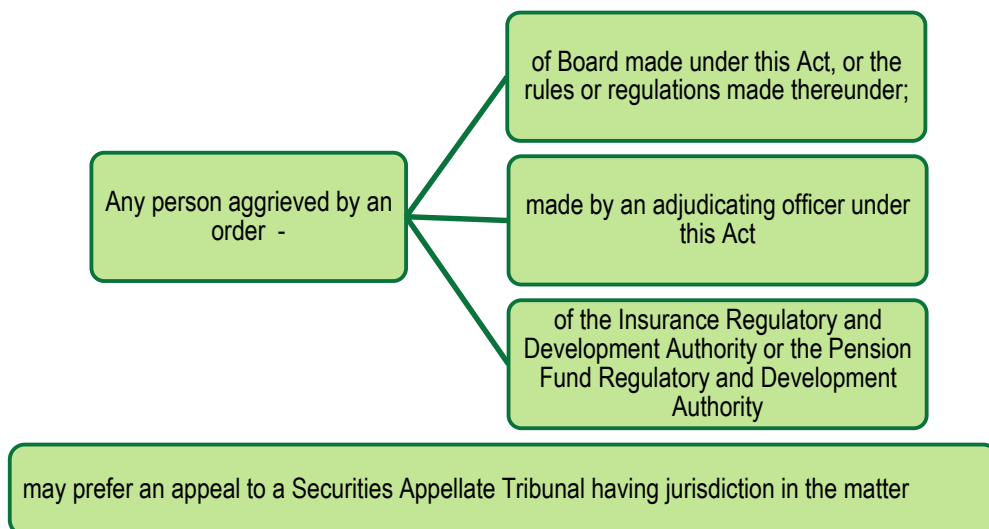
No order of the Central Government appointing any person as the Presiding Officer or a Member of a Securities Appellate Tribunal shall be called in question in any manner, and no act or proceeding before a Securities Appellate Tribunal shall be called in question in any manner on the ground merely of any defect in the constitution of a Securities Appellate Tribunal.

Staff of the Securities Appellate Tribunal [Section 15S]

- (1) The Central Government shall provide the Securities Appellate Tribunal with such officers and employees as that Government may think fit.
- (2) The officers and employees of the Securities Appellate Tribunal shall discharge their functions under general superintendence of the Presiding Officer.
- (3) The salaries and allowances and other conditions of service of the officers and employees of the Securities Appellate Tribunal shall be such as may be prescribed.

Appeal to the Securities Appellate Tribunal [Section 15T]

- (1) **Who may file an appeal**



- (2) **Time period for filing of an appeal:** Every appeal shall be filed **within** a period of **forty-five days** from the date on which a copy of the order made by the Board or the Adjudicating Officer or the Insurance Regulatory and Development Authority or the Pension Fund Regulatory and Development Authority, as the case may be, is received by him and it shall be in such form and be accompanied by such fee as may be prescribed:

Condonation of delay: Provided that the Securities Appellate Tribunal may entertain an appeal after the expiry of the said period of forty-five days if it is **satisfied** that there was **sufficient cause** for not filing it within that period.

- (3) **Order passed by SAT:** On receipt of an appeal, the Securities Appellate Tribunal may, after giving the parties to the appeal, an opportunity of being heard, pass such orders thereon as it thinks fit, **confirming, modifying or setting aside** the order appealed against.
- (4) **Forwarding of copies of order to the parties:** The Securities Appellate Tribunal shall send a copy of every order made by it to the Board, or the Insurance Regulatory and Development Authority or the Pension Fund Regulatory and Development Authority, as the case may be the parties to the appeal and to the concerned Adjudicating Officer.
- (5) **Time period for disposal of appeal:** The appeal filed before the Securities Appellate Tribunal shall be dealt with by it **as expeditiously as possible** and **endeavor** shall be made by it to dispose of the appeal finally **within six months** from the date of receipt of the appeal.

Procedure and powers of the Securities Appellate Tribunal [Section 15U]

- (1) The Securities Appellate Tribunal shall not be bound by the procedure laid down by the Code of Civil Procedure, 1908, but shall be guided by the principles of natural justice and, subject to the other provisions of this Act, and of any rules, the Securities Appellate Tribunal shall have powers to regulate their own procedure including the places at which they shall have their sittings.
- (2) The Securities Appellate Tribunal shall have, for the purposes of discharging their functions under this Act, the same powers as are vested in a civil court under the Code of Civil Procedure, 1908, while trying a suit, in respect of the following matters, namely:—
- summoning and enforcing the attendance of any person and examining him on oath;
 - requiring the discovery and production of documents;
 - receiving evidence on affidavits;
 - issuing commissions for the examination of witnesses or documents;
 - reviewing its decisions;
 - dismissing an application for default or deciding it *ex parte*;
 - setting aside any order of dismissal of any application for default or any order passed by it *ex parte*;
 - any other matter which may be prescribed.

- (3) Every proceeding before the Securities Appellate Tribunal shall be deemed to be a judicial proceeding within the meaning of sections 193 and 228, and for the purposes of section 196 of the Indian Penal Code (45 of 1860), and the Securities Appellate Tribunal shall be deemed to be a civil court for all the purposes of section 195 and Chapter XXVI of the Code of Criminal Procedure, 1973 (2 of 1974).
- (4) Where Benches are constituted, the Presiding Officer of the Securities Appellate Tribunal may, from time to time make provisions as to the distribution of the business of the Securities Appellate Tribunal amongst the Benches and also provide for the matters which may be dealt with, by each Bench.
- (5) On the application of any of the parties and after notice to the parties, and after hearing such of them as he may desire to be heard, or on his own motion without such notice, the Presiding Officer of the Securities Appellate Tribunal may transfer any case pending before one Bench, for disposal, to any other Bench.
- (6) If a Bench of the Securities Appellate Tribunal consisting of two members differ in opinion on any point, they shall state the point or points on which they differ, and make a reference to the Presiding Officer of the Securities Appellate Tribunal who shall either hear the point or points himself or refer the case for hearing only on such point or points by one or more of the other members of the Securities Appellate Tribunal and such point or points shall be decided according to the opinion of the majority of the members of the Securities Appellate Tribunal who have heard the case, including those who first heard it.

Right to legal representation [Section 15V]

The appellant may either appear in person or authorise one or more chartered accountants or company secretaries or cost accountants or legal practitioners or any of its officers to present his or its case before the Securities Appellate Tribunal.

Limitation [Section 15W]

The provisions of the Limitation Act, 1963 shall, as far as may be, apply to an appeal made to a Securities Appellate Tribunal.

Presiding Officer, Members and staff of Securities Appellate Tribunals to be public servants [Section 15X]

The Presiding Officer, Members and other officers and employees of a Securities Appellate Tribunal shall be deemed to be public servants within the meaning of section 21 of the Indian Penal Code.

Civil Court not to have jurisdiction [Section 15Y]

No civil court shall have jurisdiction to entertain any suit or proceeding in respect of any matter which an adjudicating officer appointed under this Act or a Securities Appellate Tribunal constituted under this Act is empowered by or under this Act to determine and no injunction shall be granted by any

court or other authority in respect of any action taken or to be taken in pursuance of any power conferred by or under this Act.

Appeal to Supreme Court [Section 15Z]

Any person aggrieved by any decision or order of the Securities Appellate Tribunal may-

- file an appeal to the Supreme Court **within sixty days** from the date of communication of the decision or order of the Securities Appellate Tribunal to him on any question of law arising out of such order:

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

15. MISCELLANEOUS

Power of Central Government to issue directions [Section 16]

- (1) Without prejudice to the foregoing provisions of this Act or the Depositories Act, 1996, the Board shall, in exercise of its powers or the performance of its functions under this Act, be bound by such directions on questions of policy as the Central Government may give in writing to it from time to time.

Provided that the Board shall, as far as practicable, be given an opportunity to express its views before any direction is given under this sub-section.

- (2) The decision of the Central Government whether a question is one of policy or not shall be final.

Power of Central Government to supersede the Board [Section 17(1)]

If at any time the Central Government is of opinion that Board unable to perform its functions, it may by notification, supersede the Board for such period, not exceeding six months.

Reasons to supersede the Board-

Central
government
may
supersede
the Board-

- on account of **grave emergency**, the Board is unable to discharge the functions and duties under the provisions of this Act; or
- that the **Board** has persistently **made default** in complying with any direction issued by the Central Government under this Act or
- **default in the discharge of the functions and duties** imposed under the provisions of this Act and as a result of such default the financial position of the Board or the administration of the Board has deteriorated; or
- that circumstances exist which render it necessary in the **public interest** so to do

Effect of publication of notification of superseding the Board [Section 17(2)]:

Upon the publication of a notification of superseding the Board,—

- (a) all the members shall, as from the date of supersession, vacate their offices as such;
- (b) all the powers, functions and duties which may, by or under the provisions of this Act, be exercised or discharged by or on behalf of the Board, shall until the Board is reconstituted, be exercised and discharged by such person or persons as the Central Government may direct; and
- (c) all property owned or controlled by the Board shall, until the Board is reconstituted vest in the Central Government.

Reconstitution of Board on the expiration of the period of supersession [Section 17(3)]:

On the expiration of the period of supersession specified in the notification, the Central Government may reconstitute the Board by a fresh appointment and in such case any person or persons who vacated their offices, shall not be deemed disqualified for appointment:

Provided that the Central Government may, at any time, before the expiration of the period of supersession, take action.

Complete reports and action taken to be laid before the Parliament [Section 17(4)]:

The Central Government shall cause a notification issued and a full report of any action taken under this section and the circumstances leading to such action to be laid before each House of Parliament at the earliest.

Returns and reports [Section 18]

- (1) **Furnishing of returns and reports by the Board to the Central Government:** The Board shall furnish to the Central Government at such time and in such form and manner as may be prescribed or as the Central Government may direct, such returns and statements and such particulars in regard to any proposed or existing programme for the promotion and development of the securities market, as the Central Government may, from time to time, require.
- (2) **Report of previous financial year by the Board:** the Board shall, **within ninety days** after the end of each financial year, submit to the Central Government a report in such form, as may be prescribed, giving a true and full account of its activities, policy and programmes during the previous financial year.
- (3) **Report to be presented before Parliament:** A copy of the report received under sub-section (2) shall be laid, as soon as may be after it is received, before each House of Parliament.

Appeals [Section 20]

- (1) **Appeal to Central Government:** Any person aggrieved by an order of the Board made, **before** the commencement of the Securities Laws (Second Amendment) Act, 1999, under this Act, or the rules or regulations made thereunder may prefer an appeal to the Central Government within such time as may be prescribed.

- (2) **No appeal after expiry of limitation:** No appeal shall be admitted if it is preferred after the expiry of the period prescribed therefor.

However, it is admitted after the expiry of the period prescribed if the appellant satisfies the Central Government that he had **sufficient cause** for not preferring the appeal within the prescribed period.

- (3) **Appeal shall be made in prescribed form with a copy of an order:** Every appeal made under this section shall be made in such form and shall be accompanied by a copy of the order appealed against and by such fees as may be prescribed.

- (4) The procedure for disposing of an appeal shall be such as may be prescribed.

Provided that before disposing of an appeal, the appellant shall be given a **reasonable opportunity of being heard**.

Bar of jurisdiction [Section 20A]

No order passed by the Board or the Adjudicating Officer under this Act shall be appealable except as provided in section 15T or section 20, and

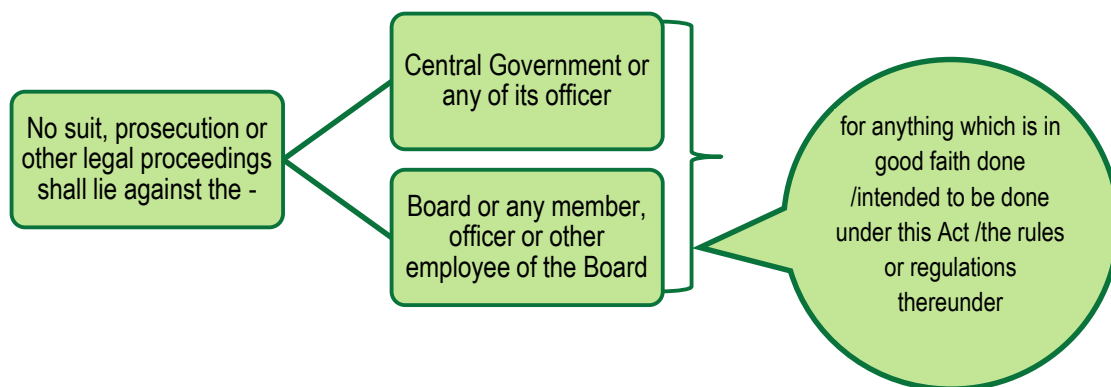
No civil court shall have jurisdiction in respect of any matter which the Board or the Adjudicating Officer is empowered by, or under, this Act to pass any order, and

No injunction shall be granted by any court or other authority in respect of any action taken or to be taken in pursuance of any order passed by the Board or the Adjudicating Officer by, or under, this Act.

Members, officers and employees of the Board to be public servants [Section 22]

All members, officers and other employees of the Board shall be deemed, when acting or purporting to act in pursuance of any of the provisions of this Act, to be public servants within the meaning of section 21 of the Indian Penal Code.

Protection of action taken in good faith [Section 23]



Offences [Section 24]

- (1) Without prejudice to any award of penalty by the adjudicating officer or the Board under this Act, if any person contravenes or attempts to contravene or abets the contravention of the provisions of this Act or of any rules or regulations made thereunder, he shall be punishable with **imprisonment** for a term which may extend to **ten years**, or with **fine**, which may extend to **twenty-five crore rupees** or with **both**.
- (2) If any person fails to pay the penalty imposed by the adjudicating officer or the Board or fails to comply with any directions or orders, he shall be punishable with **imprisonment** for a term which shall **not be less than one month** but which may **extend to ten years**, or with **fine**, which may **extend to twenty-five crore rupees** or with **both**.

Composition of certain offences [Section 24A]

Notwithstanding anything contained in the Code of Criminal Procedure, 1973, any offence punishable under this Act, not being an offence punishable with:

- imprisonment only, or
- with imprisonment **and** also with fine,

may either **before or after** the institution of any proceeding, be compounded by a Securities Appellate Tribunal or a court before which such proceedings are pending.

Power to grant immunity [Section 24B]

- (1) The **Central Government may**, on recommendation by the Board, if the Central Government is satisfied, that any person, who is alleged to have violated any of the provisions of this Act or the rules or the regulations made thereunder, has made a full and true disclosure in respect of the alleged violation,
 - **grant** to such person, subject to such conditions as it may think fit to impose, **immunity from prosecution** for any offence under this Act, or the rules or the regulations made thereunder or **also from** the imposition of any **penalty** under this Act with respect to the alleged violation.

Exception: Provided that **no such immunity** shall be granted by the Central Government in cases where the proceedings for the **prosecution** for any such offence have been **instituted before** the date of receipt of **application** for grant of such immunity.

Provided further that recommendation of the Board under this sub-section shall not be binding upon the Central Government.

- (2) **Withdrawal of granted immunity by the Central Government:** An immunity granted to a person above may, at any time, be **withdrawn by the Central Government**, if it is satisfied that:

- such person had, in the course of the proceedings, **not complied** with the **condition** on which the **immunity was granted** or
- had given **false evidence**,

and **thereupon** such person may be **tried** for the offence with respect to which the immunity was granted or for any other offence of which he appears to have been guilty in connection with the contravention **and** shall **also** become liable to the **imposition** of any penalty under this Act to which such person would have been liable, had not such immunity been granted.

Explanation – In case where the immunity is withdrawn on account of non-compliance with the conditions or false evidence, the CG or Board shall proceed with the prosecution (against which immunity was given and withdrawn) and may also impose penalty as may be required.

Cognizance of offences by courts [Section 26]

No court shall take cognizance of any offence punishable under this Act or any rules or regulations made thereunder, save on a complaint made by the Board.

Special Courts [Section 26A to Section 26D]

Establishment of Special Courts [Section 26A]

- (1) **Purpose:** The Central Government may, for the **purpose** of providing **speedy trial of offences** under this Act, by notification, establish or designate as many Special Courts as may be necessary.
- (2) **Composition:** A Special Court shall consist of a **single judge** who shall be **appointed by the Central Government with the concurrence** of the **Chief Justice of the High Court** within whose jurisdiction the judge to be appointed is working.
- (3) **Qualification:** A person shall not be qualified for appointment as a judge of a Special Court unless he is, immediately before such appointment, **holding the office** of a **Sessions Judge** or an **Additional Sessions Judge**, as the case may be.

Offences triable by Special Courts [Section 26 B]

All offences under this Act, shall be taken cognizance of and tried by:

- the Special Court **established** for the area in which the offence is committed or
- where there are **more Special Courts** than one for such area, by **such one** of them as may be **specified** in this behalf **by the High Court** concerned

Appeal and revision [Section 26C]

The High Court may exercise, so far as may be applicable, all the powers conferred by Chapters XXIX and XXX of the Code of Criminal Procedure, 1973 on a High Court, as if a Special Court within the local limits of the jurisdiction of the High Court were a Court of Session trying cases within the local limits of the jurisdiction of the High Court.

Application of Code to proceedings before Special Court [Section 26D]

- (1) Save as otherwise provided in this Act, the provisions of the Code of Criminal Procedure, 1973 shall apply to the proceedings before a Special Court and for the purposes of the said provisions, the Special Court shall be deemed to be a Court of Session and the person conducting prosecution before a Special Court shall be deemed to be a Public Prosecutor within the meaning of clause (u) of section 2 of the Code of Criminal Procedure, 1973.
- (2) The person conducting prosecution referred to in sub-section (1) should have been in practice as an advocate for not less than seven years or should have held a post, for a period of not less than seven years, under the Union or a State, requiring special knowledge of law.

Transitional provisions [Section 26E]

Any offence committed under this Act, which is triable by a Special Court shall, until a Special Court is established, be taken cognizance of and tried by a Court of Session exercising jurisdiction over the area, notwithstanding anything contained in the Code of Criminal Procedure, 1973:

Provided that nothing contained in this section shall affect the powers of the High Court under section 407 of the Code of Criminal Procedure, 1973 to transfer any case or class of cases taken cognizance by a Court of Session under this section.

Contravention by companies [Section 27]

- (1) Where a contravention of any of the provisions of this Act or any rule, regulation, direction or order made there under has been committed by a company -every person who at the time the contravention was committed was in charge of, and was responsible to, the company for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the contravention and shall be liable to be proceeded against and punished accordingly:

Exemption: This sub-section shall not render any such person liable to any punishment provided in this Act, if he proves that the contravention was committed without his knowledge or that he had exercised all due diligence to prevent the commission of such offence.

- (2) Notwithstanding anything contained in sub-section (1), where an contravention under this Act has been committed by a company and it is proved that the contravention has been committed with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of the contravention and shall be liable to be proceeded against and punished accordingly.

Explanation: For the purposes of this section,—

- (a) company means anybody corporate and includes a firm or other association of individuals; and

(b) director, in relation to a firm, means a partner in the firm.

Recovery of amounts [Section 28A]

(1) If a person **fails to pay the penalty** imposed under this Act **or fails to comply** with any **direction** of the Board **for refund of monies or fails to comply** with a direction of **disgorgement order** or fails to pay any fees due to the Board, the **Recovery Officer** may draw up under his signature a statement in the specified form specifying the amount due from the person (such statement being hereafter in this Chapter referred to as certificate) and shall proceed to recover from such person the amount specified in the certificate by one or more of the following modes, namely:—

- (a) attachment and sale of the person's **movable property**;
- (b) attachment of the person's **bank accounts**;
- (c) attachment and sale of the person's **immovable property**;
- (d) of the person and his **detention** in prison;
- (e) **appointing a receiver** for the management of the person's movable and immovable properties,

and **for this purpose, the provisions** of sections 220 to 227, 228A, 229, 232, the Second and Third Schedules to the **Income-tax Act, 1961** and the Income-tax (Certificate Proceedings) Rules, 1962, as in force from time to time, in so far as may be, **apply** with necessary modifications as if the said provisions and the rules made thereunder were the provisions of this Act and referred to the amount due under this Act instead of to income-tax under the Income-tax Act, 1961.

Explanation 1— For the purposes of this sub-section, the person's **movable or immovable property or monies held in bank accounts shall include** any property or monies held in bank accounts which has been **transferred directly or indirectly on or after the date when the amount** specified in certificate had **become due**, by the person to **his spouse or minor child or son's wife or son's minor child**, otherwise than for adequate consideration, and which is held by, or stands in the name of, any of the persons aforesaid; and so far as the movable or immovable property or monies held in bank accounts so transferred to his minor child or his son's minor child is concerned, it shall, **even after the date of attainment of majority by such minor child or son's minor child**, as the case may be, continue to be included in the person's movable or immovable property or monies held in bank accounts for recovering any amount due from the person under this Act.

Explanation 2— Any reference under the provisions of the Second and Third Schedules to the Income-tax Act, 1961 and the Income-tax (Certificate Proceedings) Rules, 1962 to the assesses shall be construed as a reference to the person specified in the certificate.

Explanation 3— Any reference to appeal in Chapter XVIII and the Second Schedule to the Income-tax Act, 1961, shall be construed as a reference to appeal before the Securities Appellate Tribunal under section 15T of this Act.

Explanation 4—The interest referred to in section 220 of the Income-tax Act, 1961 shall commence from the date the amount became payable by the person.

- (2) The Recovery Officer shall be empowered to seek the assistance of the local district administration while exercising the powers under sub-section (1).
- (3) Notwithstanding anything contained in any other law for the time being in force, the **recovery of amounts** by a Recovery Officer under sub-section (1), pursuant to non-compliance with any direction issued by the Board under section 11B, shall have precedence over any other claim against such person.
- (4) For the purposes of sub-sections (1), (2) and (3), the expression “Recovery Officer” means any officer of the Board who may be authorised, by general or special order in writing, to exercise the powers of a Recovery Officer.

Continuance of proceedings [Section 28B]

- (1) **Where a person dies**, his legal representative shall be liable to pay any sum which the deceased would have been liable to pay, if he had not died, in the like manner and to the same extent as the deceased:

Provided that, in case of any penalty payable under this Act, a legal representative shall be liable only in case the penalty has been imposed before the death of the deceased person.

- (2) For the purposes of sub-section (1),--
 - (a) any proceeding for disgorgement, refund or an action for recovery before the Recovery Officer under this Act, except a proceeding for levy of penalty, initiated against the deceased before his death shall be deemed to have been initiated against the legal representative, and may be continued against the legal representative from the stage at which it stood on the date of the death of the deceased and all the provisions of this Act shall apply accordingly;
 - (b) any proceeding for disgorgement, refund or an action for recovery before the Recovery Officer under this Act, except a proceeding for levy of penalty, which could have been initiated against the deceased if he had survived, may be initiated against the legal representative and all the provisions of this Act shall apply accordingly.
- (3) **Every legal representative shall be personally liable** for any sum payable by him in his capacity as legal representative if, while his liability for such sum remains undischarged, he creates a charge on or disposes of or parts with any assets of the estate of the deceased, which are in, or may come into, his possession, but such liability shall be limited to the value of the asset so charged, disposed of or parted with.
- (4) The liability of a legal representative under this section shall be **limited to the extent to which the estate of the deceased is capable of meeting the liability**.

Explanation.--For the purposes of this section "Legal representative" means a person who in law represents the estate of a deceased person, and includes any person who intermeddles with the estate of the deceased and where a party sues or is sued in a representative character, the person on whom the estate devolves on the death of the party so suing or sued.

Power to make rules [Section 29]

- (1) The Central Government may, by notification, make rules for carrying out the purposes of this Act.
- (2) In particular, and without prejudice to the generality of the foregoing power, such rules may provide for all or any of the following matters, namely:—
 - (a) the term of office and other conditions of service of the Chairman and the members under sub-section (1) of section 5;
 - (b) the additional functions that may be performed by the Board under section 11;
 - (c) Omitted
 - (d) the manner in which the accounts of the Board shall be maintained under section 15;
 - (da) the manner of inquiry under sub-section (1) of section 15-I;
 - (db) the salaries and allowances and other terms and conditions of service of the Presiding Officers, Members and other officers and employees of the Securities Appellate Tribunal under section 15-O and sub-section (3) of section 15S;
 - (dc) the procedure for the investigation of misbehaviour or incapacity of the Presiding Officers, or other Members of the Securities Appellate Tribunal under sub-section (3) of section 15Q;
 - (dd) the form in which an appeal may be filed before the Securities Appellate Tribunal under section 15T and the fees payable in respect of such appeal;
 - (e) the form and the manner in which returns and report to be made to the Central Government under section 18;
 - (f) any other matter which is to be, or may be, prescribed, or in respect of which provision is to be, or may be, made by rules.

Power to make regulations [Section 30]

- (1) The Board may, by notification, make regulations consistent with this Act and the rules made thereunder to carry out the purposes of this Act.
- (2) In particular, and without prejudice to the generality of the foregoing power, such regulations may provide for all or any of the following matters, namely:—

- (a) the times and places of meetings of the Board and the procedure to be followed at such meetings under sub-section (1) of section 7 including quorum necessary for the transaction of business;
- (b) the terms and other conditions of service of officers and employees of the Board under sub-section (2) of section 9;
- (c) the matters relating to issue of capital, transfer of securities and other matters incidental thereto and the manner in which such matters shall be disclosed by the companies under section 11A;
- (ca) the utilisation of the amount credited under sub-section (5) of section 11;
- (cb) the fulfilment of other conditions relating to collective investment scheme under subsection (2A) of section 11AA;]
- (d) the conditions subject to which certificate of registration is to be issued, the amount of fee to be paid for certificate of registration and the manner of suspension or cancellation of certificate of registration under section 12.
- (da) the terms determined by the Board for settlement of proceedings under sub-section (2) and the procedure for conducting of settlement proceedings under sub-section (3) of section 15JB;
- (db) any other matter which is required to be, or may be, specified by regulations or in respect of which provision is to be made by regulations.

Rules and regulations to be laid before Parliament [Section 31]

Every rule and every regulation made under this Act shall be laid, as soon as may be after it is made, before each House of Parliament, while it is in session, for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the rule or regulation or both Houses agree that the rule or regulation should not be made, the rule or regulation shall thereafter have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that rule or regulation.

Application of other laws not barred [Section 32]

The provisions of this Act shall be in addition to, and not in derogation of, the provisions of any other law for the time being in force.

Power to remove difficulties [Section 34]

- (1) If any difficulty arises in giving effect to the provisions of this Act, the Central Government may, by order, published in the Official Gazette, make such provisions not inconsistent with the provisions of this Act as may appear to be necessary for removing the difficulty:

Provided that no order shall be made under this section after the expiry of five years from the commencement of this Act.

- (2) Every order made under this section shall be laid, as soon as may be after it is made, before each House of Parliament.

Validation of certain acts [Section 34A]

34A. Any act or thing done or purporting to have been done under the principal Act, in respect of calling for information from, or furnishing information to, other authorities, whether in India or outside India, having functions similar to those of the Board and in respect of settlement of administrative and civil proceedings, shall, for all purposes, be deemed to be valid and effective as if the amendments made to the principal Act had been in force at all material times.

SEBI (LISTING OBLIGATIONS AND DISCLOSURE REQUIREMENTS) REGULATIONS, 2015

INDEX

S.No.	Particulars
1	Scope and Introduction
2	Common Obligations of Listed Entities
3	Quarterly Compliances
4	Annual Compliances
5	Corporate Governance
6	Committees Under LODR Regulations



1. SCOPE

On September 2, 2015, SEBI notified the Listing Obligations and Disclosure Requirements Regulations, 2015 to be called as the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 .

The objective of this Regulation is firstly, to align clauses of the listing agreement with Companies Act and secondly, to consolidate the conditions under different securities' listing agreements into one single regulation. This Regulation is applicable to any entity (whether a company or not) accessing the stock exchange, for listing equity shares (on main board, SME exchange, institutional trading platforms), debt securities, preference shares, depository receipts, securitized debt instruments, mutual fund units, and other securities as may be specified by SEBI.



2. INTRODUCTION

Securities and Exchange Board of India (SEBI), on September 2, 2015, issued SEBI (Listing and Disclosure) Regulations, 2015 on listing of different segments of the capital market and disclosure norms in relation thereto. The Regulation became effective from December 1, 2015.

These regulations have been structured into single document with the aim to consolidate and streamline the provision of existing listing agreements for different segments of capital markets, such as equity shares (including convertibles), non-convertible debt securities, etc. for ensuring better enforceability.

The latest set of norms provides broad principles for periodic disclosures by listed entities, apart from incorporating corporate governance principles.

Applicability: These regulations shall apply to a listed entity which has listed any of the following designated securities on recognized stock exchange(s):

- Specified securities listed on main board or SME Exchange or Innovators Growth Platform;
- Non-convertible debt securities,
- Indian depository receipts;
- Securitized debt instruments;
- Security Receipts;
- Units issued by mutual funds;
- Any other securities as may be specified by the Board.

(2) The provisions of these regulations which become **applicable to listed entities on the basis of market capitalisation criteria** shall continue to apply to such entities even if they fall below such thresholds.

(3) The provisions of these regulations which become **applicable to listed entities on the basis of the criterion of the value of outstanding listed debt securities** shall continue to apply to such entities even if they fall below such thresholds as mentioned in sub-regulation (1A) of regulation 15.



3. REGULATIONS

The Listing Regulations have been sub-divided into two parts viz,:

- (a) **Substantive** provisions incorporated in the main body of Regulations,
- (b) **Procedural** requirements in the form of schedules to the Regulations

Board of Directors [Regulation 17]

(1) **Composition of Board:** The composition of board of directors (BOD) of the listed entity shall be as follows:

- a. BOD shall have an **optimum combination of executive and non-executive directors** with **at least one-woman director** and **not less than 50%** of the BOD shall comprise of **non-executive directors**.

Provided that the BOD of the **top 1000 listed entities** (determined on the basis of market capitalisation, as at the end of the immediate previous financial year) shall have **at least one independent woman director** by April 1, 2020

- b. where the **chairperson** of the BOD is a **non-executive director**, **at least one-third** of the BOD shall comprise of **independent directors** and where the **chairperson** of the BOD is not a regular non-executive chairperson, **at least half** of the BOD shall comprise of **independent directors**.

Provided that where the regular non-executive chairperson is a promoter of the listed entity or is "related to any promoter" or person occupying management positions at the level of BOD or at one level below the BOD - at least half of the BOD of the listed entity shall consist of independent directors.

For the purpose of this clause, "related to any promoter" means:

- (i) If the **promoter is a listed entity**, its directors **other than the independent directors**, its employees or its nominees shall be deemed to be related to it;
- (ii) If the **promoter is an unlisted entity**, its directors, its employees or its nominees shall be deemed to be related to it.

Provisions relating to independent directors are not applicable to section 8 (licensed i.e. non-profit) companies [MCA Notification dated 5-6-2015 issued under section 462 of Companies Act, 2013]

- c. The BOD of the top 2000 listed entities (with effect from April 1, 2020) shall **comprise of not less than six directors**.

Age limit: No listed entity shall appoint a person or continue the directorship of any person as a non-executive director who has attained the age of **seventy-five years** unless a special resolution is passed to that effect, in which case the explanatory statement annexed to the notice for such motion shall indicate the justification for appointing such a person.

(2) **Board meetings and information to be given to Board:** The BOD shall meet **at least four times** in a year, with maximum time gap of 120 days between any two meetings.

The quorum for every meeting of the BOD of the **top 2000 listed entities** with effect from April 1, 2020 shall be **one-third** of its total strength **or three** directors, whichever is **higher**, **including at least one independent director**.

- (3) **Review of compliance report** – The Board will periodically review compliance reports of all laws applicable to company, prepared by company and steps taken by company to rectify instances of non-compliance.
- (4) The evaluation of independent directors shall be done by the **entire board of directors** which shall include:
 - a. performance of the directors; **and**
 - b. fulfillment of the independence criteria as specified in these regulations and their independence from the management:

Provided that in the above evaluation, the directors who are subject to evaluation shall not participate.

Maximum Number of Directorship [Regulation 17A]

The directors of listed entities shall comply with the following conditions with respect to the maximum number of directorships, **including any alternate directorships** that can be held by them at any point of time -

- (1) A person shall **not be a director in more than seven listed entities** w.e.f. April 1, 2020.
Provided that a person shall **not** serve as an **independent director in more than seven listed entities**.
- (2) Notwithstanding the above, any person who is serving as a whole time director / managing director in any listed entity shall serve as an **independent director** in not more than **three listed entities**.

Explanation: For the purpose of this Regulation, the count for the number of listed entities on which a person is a director / independent director shall be only those whose equity shares are listed on a stock exchange

Restriction on number of memberships [Regulation 26]

- (1) A director shall not be a **member** in more than **ten committees** or act as **chairperson** of more than **five committees** across **all listed entities** in which he/she is a director which shall be determined as follows:
 - a. the limit of the committees on which a director may serve in all **public limited companies**, whether listed or not, **shall be included** and all **other companies** including private limited companies, foreign companies, **high value debt listed entities** and companies under Section 8 of the Companies Act, 2013 **shall be excluded**;

- b. for the purpose of determination of limit, chairpersonship and membership of the **audit committee and the Stakeholders' Relationship Committee alone** shall be considered.
- (2) Every director shall **inform the listed entity** about the committee positions he or she occupies in other listed entities and notify changes as and when they take place.

Corporate Governance Requirement with respect to Subsidiary Companies of Listed Company [Regulation 24]

- (1) At least one independent director on the board of directors of the listed entity shall be a director on the board of directors of an unlisted **material subsidiary**, whether incorporated in India or not.

The term "material subsidiary" shall mean a subsidiary, whose income or net worth exceeds twenty percent of the consolidated income or net worth respectively, of the listed entity and its subsidiaries in the immediately preceding accounting year.

- (2) The Audit Committee of the listed company shall also **review the financial statements**, in particular the investments made by the subsidiary company.
- (3) The **minutes of the Board meetings** of the unlisted subsidiary shall be placed at the meeting of the BOD of the listed entity.
- (4) The Management of the unlisted subsidiary should bring to notice of Board of listed entity, a statement of all **significant transactions** and arrangements entered into by unlisted subsidiary.

Explanation.- For the purpose of this regulation, the term "significant transaction or arrangement" shall mean any individual **transaction** or arrangement **that exceeds** or is likely to exceed **10% of the total** revenues or total expenses or total assets or total liabilities, as the case may be, of the unlisted subsidiary for the immediately preceding accounting year.

- (5) A listed entity shall **not dispose of shares** in its **material subsidiary** resulting in reduction of its shareholding (either on its own or together with other subsidiaries) **to less than or equal to 50%** or cease the exercise of control over the subsidiary **without passing a special resolution** in its General Meeting.

However, no such special resolution would be required in cases where:

- such divestment is made under a scheme of arrangement duly approved by a Court/Tribunal or under a resolution plan duly approved under section 31 of the Insolvency Code **and**
- such an event is **disclosed** to the recognized stock exchanges **within one day** of the resolution plan being approved.

- (6) **Selling, disposing and leasing of assets** amounting to **more than 20%** of the assets of the **material subsidiary** on an aggregate basis during a financial year shall require **prior approval** of shareholders by way of **special resolution**

However, no such special resolution would be required in cases where:

- the sale/disposal/lease is made under a scheme of arrangement duly approved by a Court/Tribunal or under a resolution plan duly approved under section 31 of the Insolvency Code **and**
- such an event is disclosed to the recognized stock exchanges within one day of the resolution plan being approved.

Where a listed entity has a listed subsidiary, which is itself a holding company, the provisions of this regulation shall apply to the listed subsidiary in so far as its subsidiaries are concerned.

I. Corporate Governance Report [Schedule V of the Regulation]

The annual report shall contain additional disclosures relating to Corporate Governance. The following disclosures shall be made in the section on the corporate governance of the annual report, inter-alia:

- (1) A brief statement on listed entity's **philosophy** on code of governance
- (2) **Board of Directors:** The following shall be disclosed, inter-alia,
 - a. Composition and category of directors (e.g., promoter, executive, non-executive, independent non-executive, nominee director - institution represented and whether as lender or as equity investor.
 - b. attendance of each director at the BOD meetings and the last AGM
 - c. number of other BOD or Committees in which director is a member or Chairperson
 - d. number of BOD meetings held and dates on which held
 - e. disclosures between directors inter-se
- (3) **Audit Committee:**
 - a. Brief description of terms of reference
 - b. composition, name of members and chairperson
 - c. meetings and attendance during the year.
- (4) **Nomination and Remuneration Committee:**
 - a. brief description of terms of reference
 - b. composition, name of members and chairperson

- c. meetings and attendance during the year
- d. performance evaluation criteria for independent directors
- (5) **Stakeholders' relationship committee**
 - a. name of the non-executive director heading the committee;
 - b. name and designation of the compliance officer;
 - c. number of shareholders' complaints received during the financial year;
 - d. number of complaints not solved to the satisfaction of shareholders;
 - e. number of pending complaints.
- (5A) **Risk management committee:**
 - a. brief description of terms of reference;
 - b. composition, name of members and chairperson;
 - c. meetings and attendance during the year;"
- (6) **General Body meetings:**
 - a. location and time, where last three AGMs held
 - b. whether any special resolutions passed in the previous 3 AGMs
 - c. whether any special resolution passed last year through postal ballot - details of voting pattern
 - d. person who conducted the postal ballot exercise
 - e. whether any special resolution is proposed to be conducted through postal ballot
 - f. procedure for postal ballot
- (7) **Other disclosures** shall include, inter-alia, :
 - a. disclosures on materially significant related party transactions that may have potential conflict with the interests of company at large
 - b. details of non-compliance by the listed entity, penalties, strictures imposed on the entity by stock exchange or SEBI or any statutory authority, on any matter related to capital markets, during the last 3 years
 - c. details of establishment of whistle Blower policy and affirmation that no personnel has been denied access to the audit committee
 - d. details of compliance with mandatory requirements and adoption of non-mandatory requirements of clause 49.

II. Performance Evaluation of the Board and its directors:

Companies Act, 2013 and SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 make provisions relating to evaluation of performance of (i) Board (ii) Individual directors and Chairperson and (iii) Committees of Board (specially Nomination and Remuneration Committee).

Following provision of the Companies Act, 2013 talks about evaluation:

- a) Section 134(3) requires statement of annual evaluation by Board of its own performance and of committees.
- b) Section 178(2) requires Nomination and Remuneration Committee to identify persons to be directors
- c) Schedule IV talks about performance evaluation of independent directors

Similarly, SEBI (LODR) Regulations also covers provisions relating to functions of Board, performance evaluation of directors, role of Nomination and Remuneration Committee and Corporate Governance Report.

**4. COMMON OBLIGATIONS OF LISTED ENTITIES****General Obligation of Compliance [Regulation 5]**

The listed entity shall ensure that key managerial personnel (KMP), directors, and promoters or any other person dealing with the listed entity, complies with responsibilities or obligations, if any, assigned to them under these regulations.

Compliance officer and his/her obligation [Regulation 6]

- (1) A listed entity shall appoint a qualified company secretary as the compliance officer.
- (2) The Compliance officer so appointed shall be responsible for:
 - a. ensuring conformity with the regulatory provisions applicable to the listed entity in letter and spirit,
 - b. co-ordination and reporting to the Board,
 - c. ensuring that correct procedures have been followed that would result in correctness of information filed by listed entity under the regulations and
 - d. monitoring email address of grievance redressal division.

Share Transfer Agent [Regulation 7]

The listed entity shall appoint a share transfer agent or manage the share transfer facility in house.



5. QUARTERLY COMPLIANCES

A listed entity shall, inter-alia, make the following filings with the Recognised Stock Exchange(s) on a quarterly basis:

A. Regulation 13(3): Grievance Redressal Mechanism

The listed entity shall file with the recognized stock exchange(s) on a quarterly basis, within **21 days** from the end of each quarter, a statement giving the number of investor complaints pending at the beginning of the quarter, those received during the quarter, disposed of during the quarter and those remaining unresolved at the end of the quarter.

B. Regulation 27(2):- Other Corporate Governance Requirements

A listed entity shall submit quarterly compliance report on corporate governance in the format as specified by the Board from time to time to the recognized stock exchange(s) within **21 days** from **the end of each** the quarter.

C. Regulation 31(1): Holding of Specified Securities and Shareholding Pattern.

A listed entity shall submit a statement showing holding of securities and shareholding pattern separately for each class of securities:-

- (a) **One day** prior to listing of its securities on the stock exchange(s);
- (b) On a quarterly basis, **within 21 days** from the end of each quarter; and,
- (c) Within **10 days** of any capital restructuring of the listed entity resulting in a change exceeding **2% per cent** of the total paid-up share capital.

D. Regulation 32(1): Statement of Deviation(S) Or Variation(S)

A listed entity shall submit to the stock exchange the following statement(s) on a quarterly basis for public issue, rights issue, preferential issue etc.,;

- (a) **indicating deviations**, if any, in the use of proceeds from the objects stated in the offer document or explanatory statement to the notice for the general meeting, as applicable;
- (b) **indicating category wise variation** (capital expenditure, sales and marketing, working capital etc.) between projected utilization of funds made by it in its offer document or explanatory statement to the notice for the general meeting, as applicable and the actual utilization of funds.

E. Regulation 33(3): Financial Results

The listed entity shall submit quarterly and year-to-date standalone financial results to the stock exchange **within 45 days** of end of each quarter, other than the last quarter.

Summary of above quarterly compliances:

Within ___ days from the end of each the quarter	Statement / Reports to be filed with RSE by Listed Entity
21 days	Report on Corporate Governance in format specified by BOD
21 days	Statement showing number of investor complaint : 1. Pending at the beginning of the quarter 2. Received during the quarter. 3. Disposed of during the quarter. 4. Remaining unresolved during the quarter
21 days	Statement showing holding of securities and shareholding pattern separately for each class of securities. (Also, to be disclosed one day prior to listing and within 10 days of any capital restructuring scheme of the listed entity resulting in change >2% of the total PUSC)
45 days (other than last quarter)	Quarterly and YTD standalone financial statement
For such period till which the issues proceeds are fully utilized or purpose achieved	Quarterly statement for public issue, right issues, preferential issues , etc. a. indicating deviations in the use of proceeds from the objects stated in offer documents or ES to the notice of GM b. indicating variations (category wise such as Capex, Sales and Marketing, working capital, etc.) between projected utilization of fund made in OD / ES to notice of GM vs actual utilization of fund



6. PRIOR INTIMATION OF BOARD MEETING

A. Prior Intimation of Board Meetings [Regulation 29(1) and 29(2)]

The listed entity shall give prior intimation to stock exchange about the meeting of the board of directors in following cases:

- At least **5 days** in advance (excluding date of meeting and date of intimation) in which the financial results viz. quarterly, half yearly, or annual, as the case may be, is due to be considered.
- At least **2 working days** in advance, excluding the date of the intimation and date of the meeting in case where any of the following proposal is due to be considered:

- proposal for **buyback** of securities;
- proposal for **voluntary delisting** by the listed entity from the stock exchange(s);
- **fund raising** by way of further public offer, rights issue, American Depository Receipts/Global Depository Receipts/Foreign Currency Convertible Bonds, qualified institutions placement, debt issue, preferential issue or any other method and for determination of issue price;
- **declaration/recommendation of dividend**, issue of convertible securities including convertible debentures or of debentures carrying a right to subscribe to equity shares or the passing over of dividend;
- the proposal for **declaration of bonus securities**;

B. Prior Intimation for alteration of securities [Regulation 29(3)]

The listed entity shall give intimation to the stock exchange(s) at least **11 working days** before any of the following proposal is placed before the board of directors:

- Any alteration in the **form or nature** of any of its securities that are listed on the stock exchange or in the rights or privileges of the holders thereof.
- Any alteration in the **date** on which, the interest on debentures or bonds, or the redemption amount of redeemable shares or of debentures or bonds, shall be payable.

C. Record Date or Date of Closure of Transfer Books [Regulation 42(2)]

The listed entity shall give notice in advance of at least **7 working days** (excluding the date of intimation and the record date) to stock exchange(s) of **record date** specifying the **purpose** of the record date.

The record date could be for any of the following event:

- declaration of dividend;
- issue of right or bonus shares;
- issue of shares for conversion of debentures or any other convertible security;
- shares arising out of rights attached to debentures or any other convertible security
- corporate actions like mergers, de-mergers, splits, etc;
- such other purposes as may be specified by the stock exchange(s).

D. Regulation 42(3): Dividend

A listed entity shall recommend or declare all dividend and/or cash bonuses at least **5 working days** (excluding the date of intimation and the record date) before the record date.

E. Regulation 46(3):- Website

A listed entity shall update any change in the content of its website **Within 2 working days** from the date of such change in content.

Summary of above prior intimations to RSEs:

Intimation to RSE at least ___ days before meeting (excluding date of intimation & date of meeting)	Where the following proposal is due to be covered in the BOD meeting:
2 working days	• Proposal for buyback of securities • Proposal for voluntary delisting • Fund raising by way of FPO, ADR, GDR, Convertible Bonds, Debt issue, preferential issues, etc. • Declaration / Recommendation to declare dividend • Issuance of convertible securities incl. convertible debentures. • Declaration of bonus securities where such proposal is communicated to the board of directors of the listed entity as part of the agenda papers;
5 days	Financial Results
7 working days prior to record date	Notice of Record date and the purpose of record date
11 working days	• Alteration in form of securities or rights of the holder thereof • Alteration in date on which the interest or redeemable amount of debenture will be payable

**7. ANNUAL / YEARLY COMPLIANCES**

The annual/yearly compliances that have to be followed are as follows:

- A. Regulation 33(3): Financial Results:** The listed entity shall submit **annual audited standalone** financial results for the financial year, along with the audit report and Statement on Impact of Audit Qualifications (applicable only for audit report with modified opinion), **within 60 days** from the end of Financial Year.
- B. Regulation 34: Annual Report:** The listed entity shall submit to the stock exchange and publish on its website:
- a copy of the annual report sent to the shareholders along with the notice of the annual general meeting **not later than the day of commencement of dispatch** to its shareholders;

- (b) in the event of any changes to the annual report, the **revised copy** along with the details of and explanation for the changes shall be sent **not later than 48 hours** after the annual general meeting.

Regulation 36(2): Documents & Information to Shareholders: A listed entity shall send annual report to the holders of securities not less than **21 days before** the Annual General Meeting.

Summary of above annual compliances:

Time Limit	Compliance with Stock Exchange
Within 60 days from end of FY	Entity to submitted AUDITED standalone financial results for the FY along with audit report and Statement on Impact of Audit Qualifications (applicable only for audit report with modified opinion)
Not later than the day of commencement of its dispatch to shareholder	Submit to stock exchange + Publish on website – A copy of annual report sent to shareholders along with notice for AGM
Within 48 hours of AGM	In the event of any changes to Annual Report , revised copy along with detailed explanation for such changes



8. CORPORATE GOVERNANCE

Approval for related party transactions through a resolution.

- All existing material related party contracts / arrangements, prior to the date of notification of these Regulations, and which may continue beyond, to be placed for approval of the shareholders in first General Meeting subsequent to notification of these Regulations.

Compliance Report on Corporate Governance

The following reports are submitted to Stock Exchange:-

- Quarterly Compliance Report** – to be submitted within **15 days** from end of quarter
- Annual Compliance Report** to be submitted **within 6 months** from the end of financial year – may be submitted along with second quarter report.

Related Party Transactions (Regulation 23)

As per Regulation 2(1) (zb) “**related party**” means a related party as defined under sub-section (76) of section 2 of the Companies Act, 2013 or under the applicable accounting standards.

Provided that:

- any person or entity forming a part of the promoter or promoter group of the listed entity; or
- any person or any entity, holding equity shares:

- I. of twenty per cent or more, or
- II. of ten per cent or more, with effect from April 1, 2023

in the listed entity either directly or on a beneficial interest basis as provided under section 89 of the Companies Act, 2013, at any time, during the immediate preceding financial year, shall be deemed to be a related party.

However, this definition shall not be applicable for the units issued by mutual funds which are listed on a recognised stock exchange(s).

As per Regulation 2(1)(zc), **related party transaction** means a transaction involving a transfer of resources, services or obligations between:

- (i) a listed entity or any of its subsidiaries on one hand and a related party of the listed entity or any of its subsidiaries on the other hand; or
- (ii) a listed entity or any of its subsidiaries on one hand, and any other person or entity on the other hand, the purpose and effect of which is to benefit a related party of the listed entity or any of its subsidiaries, with effect from April 1, 2023

regardless of whether a price is charged and a “transaction” with a related party shall be construed to include a single transaction or a group of transactions in a contract:

Following shall not be a related party transaction:

- (a) the issue of specified securities on a preferential basis, subject to compliance of the requirements under the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018;
- (b) the following corporate actions by the listed entity which are uniformly applicable/offered to all shareholders in proportion to their shareholding:
 - i. payment of dividend;
 - ii. subdivision or consolidation of securities;
 - iii. issuance of securities by way of a rights issue or a bonus issue; and
 - iv. buy-back of securities.
- (c) acceptance of fixed deposits by banks/Non-Banking Finance Companies at the terms uniformly applicable/offered to all shareholders/public, subject to disclosure of the same along with the disclosure of related party transactions every six months to the stock exchange(s), in the format as specified by the SEBI.

However, this definition shall not be applicable for the units issued by mutual funds which are listed on a recognised stock exchange(s).

Under the Companies Act, 2013

According to section 2 (76) "related party", with reference to a company, means –

- (i) a director or his relative;
- (ii) a key managerial personnel or his relative;
- (iii) a firm, in which a director, manager or his relative is a partner;
- (iv) a private company in which a director or manager or his relative is a member or director;
- (v) a public company in which a director or manager is a director and holds or holds along with his relatives, more than two per cent of its paid-up share capital;
- (vi) any body corporate whose Board of Directors, managing director or manager is accustomed to act in accordance with the advice, directions or instructions of a director or manager;
- (vii) any person on whose advice, directions or instructions a director or manager is accustomed to act;

However, nothing in sub-clauses (vi) and (vii) shall apply to the advice, directions or instructions given in a professional capacity;

- (viii) Any body corporate which is –
 - (A) a holding, subsidiary or an associate company of such company;
 - (B) a subsidiary of a holding company to which it is also a subsidiary; or
 - (C) an investing company or the venturer of the company;

Explanation. – For the purpose of this clause, "the investing company or the venturer of a company" means a body corporate whose investment in the company would result in the company becoming an associate company of the body corporate.

- (ix) a director other than an independent director or key managerial personnel of the holding company or his relative with reference to a company, shall be deemed to be a related party.

Material Related Party Transaction

A transaction with a related party shall be considered material, if the transaction(s) to be entered into individually or taken together with previous transactions during a financial year, exceeds rupees one thousand Crore or ten percent of the annual consolidated turnover of the listed entity as per the last audited financial statements of the listed entity whichever is lower.

A transaction involving payments made to a related party with respect to brand usage or royalty shall be considered material if the transaction(s) to be entered into individually or taken together with previous transactions during a financial year, exceed five percent of the annual consolidated turnover of the listed entity as per the last audited financial statements of the listed entity.

Approval of Audit Committee

All related party transactions and subsequent material modifications shall require prior approval of the audit committee of the listed entity.

However, only those members of the audit committee, who are independent directors, shall approve related party transactions.

Omnibus Approval: Audit committee may grant omnibus approval for related party transactions proposed to be entered into by the listed entity subject to the following conditions-

- (a) the audit committee shall lay down the criteria for granting the omnibus approval in line with the policy on related party transactions of the listed entity and such approval shall be applicable in respect of transactions which are repetitive in nature;
- (b) the audit committee shall satisfy itself regarding the need for such omnibus approval and that such approval is in the interest of the listed entity;
- (c) the omnibus approval shall specify:
 - (i) the name(s) of the related party, nature of transaction, period of transaction, maximum amount of transactions that shall be entered into;
 - (ii) the indicative base price / current contracted price and the formula for variation in the price if any; and
 - (iii) such other conditions as the audit committee may deem fit.

However, where the need for related party transaction cannot be foreseen and aforesaid details are not available, audit committee may grant omnibus approval for such transactions subject to their value not exceeding rupees one crore per transaction.

- (d) the audit committee shall review, at least on a quarterly basis, the details of related party transactions entered into by the listed entity pursuant to each of the omnibus approvals given.
- (e) Such omnibus approvals shall be valid for a period not exceeding one year and shall require fresh approvals after the expiry of one year.

Approval of the shareholders

All material related party transactions and subsequent material modifications as defined by the audit committee shall require prior approval of the shareholders through resolution and no related party shall vote to approve such resolutions whether the entity is a related party to the particular transaction or not.

However, the requirements specified above shall not apply in respect of a resolution plan approved under section 31 of the Insolvency Code, subject to the event being disclosed to the recognized stock exchanges within one day of the resolution plan being approved.

Exceptions

The approval of Audit committee and shareholders shall not be required in the following cases:

- (a) transactions entered into between two government companies;
- (b) transactions entered into between a holding company and its wholly owned subsidiary whose accounts are consolidated with such holding company and placed before the shareholders at the general meeting for approval;
- (c) transactions entered into between two wholly-owned subsidiaries of the listed holding company, whose accounts are consolidated with such holding company and placed before the shareholders at the general meeting for approval.

Government Company(ies) means Government Company as defined in sub-section (45) of section 2 of the Companies Act, 2013.

Secretarial Audit and Secretarial Compliance Report [Regulation 24A]

- (a) Every listed entity and its material unlisted subsidiaries incorporated in India shall undertake secretarial audit and shall annex a secretarial audit report given by a company secretary in practice, in such form as specified, with the annual report of the listed entity.
- (b) Every listed entity shall submit a secretarial compliance report in such form as specified, to stock exchanges, within sixty days from end of each financial year.



9. TYPES OF COMMITTEES UNDER LODR REGULATIONS

A. Audit Committee [Regulation 18]:

Every listed entity shall constitute a qualified and independent audit committee in accordance with the term of reference which shall have:

- (a) The audit committee shall have minimum **three** directors as members.
- (b) Atleast **Two-thirds** of the members of audit committee shall be independent directors.
- (c) **All** members of audit committee shall be **financially literate** and **at least one member** shall have accounting or related financial management **expertise**.
- (d) The chairperson of the audit committee shall be an **Independent Director** and he/she shall be present at Annual general meeting to answer shareholder queries.
- (e) The Company Secretary shall act as the secretary to the audit committee.
- (f) The audit committee at its discretion shall invite the finance director or head of the finance function, head of internal audit and a representative of the statutory auditor and any other such executives to be present at the meetings of the committee.

Meetings of Audit Committee:

- (a) The audit committee **shall meet** at least **four** times in a year and not more than **120** days shall elapse between two meetings.
- (b) The **quorum** for audit committee meeting shall either be **two** members or **one third** of the members of the audit committee, whichever is greater, with at least **2** Independent directors.
- (c) The audit committee shall have **powers to investigate any activity** within its terms of reference, seek information from any employee, obtain outside legal or other professional advice and secure attendance of outsiders with relevant expertise, if it considers necessary.

Comparison of Audit Committee as per LODR vs Sec 177 of Companies Act, 2013

Particulars	As per LODR	As per Sec 177 of the Companies Act, 2013
Applicable to	All listed companies	• All Listed Companies • Unlisted Public Co. with: • Paid up share capital ≥ 10 cr or • Outstanding loans, borrowings or debentures > 50 crore or • Turnover ≥ 100 crore *Limit once applicable to apply for 3 consecutive years
Min. no. of directors	3	3
Min. Independent directors	2/3 rd	Majority
Financial Literacy	All	Majority including chairperson
Chairperson	Chairperson shall be ID and has to be present at the AGM	To be financially literate
Secretary	CS of co. to be the secretary	No such provisions
Meetings	At least 4 times in a year with a maximum gap of 120 days	No such provisions

Quorum	2 or 1/3 rd , whichever is higher with minimum 2 ID to be present	No such provisions
Additional requirements	The committee may invite finance executives to the meeting.	No such provision

B. Nomination and Remuneration Committee [Regulation 19]:

The Board of directors shall constitute the nomination and remuneration committee as follows:

- The committee shall comprise of **at least 3** directors;
- All directors of the committee shall be **Non-Executive Directors**; and
- At least **two-thirds** of the directors shall be independent directors.
- The **Chairperson** of this committee shall be an independent director:

Provided that the **chairperson of the listed entity**, whether executive or non-executive, may be **appointed as a member** of the Nomination and Remuneration Committee and shall not chair such Committee.

- The Chairperson of this committee may be present at the annual general meeting, to answer the shareholders' queries; however, it shall be up to the chairperson to decide who shall answer the queries

Meetings of Nomination and Remuneration Committee:

- (a) The nomination and remuneration committee shall meet at least once in a year.
- (b) The **quorum** for a meeting shall be either **two members** or **one third** of the members of the committee, whichever is greater, including at least **one** independent director in attendance.

C. Stakeholders Relationship Committee [Regulation 20]:

The listed entity shall constitute a Stakeholders Relationship Committee to specifically look into various aspects of interest of shareholders, debenture holders and other security holders.

Features of this committee is as follows:

- The Chairperson of this committee shall be a **Non-Executive director**.
- **At least three directors**, with at least one being an independent director, shall be members of the Committee.

- The **Chairperson** of this Committee shall **be present at the annual general meetings** to answer queries of the security holders.
- The stakeholder's relationship committee shall meet **at least once in a year**.

D. Risk Management Committee

- The Board of directors shall constitute a Risk Management Committee.
- The Risk Management Committee shall have **minimum three members with majority of them being members of the board of directors**, including **at least one independent director** and in case of a listed entity having outstanding SR (Superior voting Rights) equity shares, at least two thirds of the Risk Management Committee shall comprise independent directors.
- The Chairperson of the Risk management committee shall be a member of the board of directors and senior executives of the listed entity may be members of the committee.
- The risk management committee shall **meet at least twice** in a year.
- The **quorum** for a meeting of the Risk Management Committee shall be **either two members or one third of the members of the committee, whichever is higher**, including at least one member of the board of directors in attendance.
- The meetings of the risk management committee shall be conducted in such a manner that **on a continuous basis not more than one hundred and eighty days shall elapse between any two consecutive meetings**.
- The **Board of directors shall define the role and responsibility** of the Risk Management Committee and may delegate monitoring and reviewing of the risk management plan to the committee and such other functions as it may deem fit such function shall specifically cover cyber security.

Provided that the role and responsibilities of the Risk Management Committee shall mandatorily include the performance of functions specified in Part D of Schedule II.

The provisions of this regulation shall be **applicable** to:

- the top 1000 listed entities, determined on the basis of market capitalization as at the end of the immediate preceding financial year; and,
 - a 'high value debt listed entity'.
- The Risk Management Committee shall **have powers to seek information from any employee**, obtain outside legal or other professional advice and secure attendance of outsiders with relevant expertise, if it considers necessary.

Summary of all the committees

	Audit Committee	Nomination and Remuneration Committee	Stakeholder Committee	Risk Management Committee (Applicable to Top 500 cos.)
Number of members	Minimum 3	At least 3, All NED (Non-executive Director)	Min. 3 directors	majority of members
Number of ID	2/3 rd	At least 50%	At least 1	At least 2/3 rd
Chairperson	ID	ID	NED	Has to be member of BOD
Meeting	At least 4 Max gap 120 days	At least once in a year	At least once in a year	At least once in a year
Quorum	Higher of 1/3 rd or 2 members At least 2 ID mandatory	Higher of 1/3 rd or 2 members At least 1 ID mandatory	Not mentioned in Regulation	Not mentioned in Regulation
Additional Points	All Members – Financial Literate At least 1 member – Financial Mgt. expertise	Chairperson of co. may be appointed as member but not chair NRC	This committee looks into complaints of the investors	Senior Executives (Non-director) may be a member

Contravention of Regulations

The listed entity or any other person thereof who contravenes any of the provisions of these SEBI (LODR) regulations, shall, in addition to liability for action in terms of the securities laws, be liable for the following actions by the respective stock exchange(s), in the manner specified in circulars or guidelines issued by the SEBI:

- imposition of fines;
- suspension of trading;
- freezing of promoter/promoter group holding of designated securities, as may be applicable, in coordination with depositories;
- any other action as may be specified by the SEBI from time to time.

SECURITIES AND EXCHANGE BOARD OF INDIA (ISSUE OF CAPITAL AND DISCLOSURE REQUIREMENTS) REGULATIONS, 2018

INTRODUCTION

SEBI(ICDR) Regulations are meant to regulate the growth and development of the Indian capital markets and at the same time balancing the interests of investors and the 'issuer companies.

Classifications of issues: Primarily, issues made by an Indian company can be classified as Public, Rights, Bonus and Private Placement.

Public issue	When an issue / offer of shares or convertible securities is made to new investors for becoming part of shareholders' family of the issuer (Entity making an issue is referred as "Issuer") it is called a public issue. Public issue means an initial public offer (IPO) or a further public offer (FPO): (i) Initial public offer (IPO): means an offer of specified securities by an unlisted issuer to the public for subscription and includes an offer for sale of specified securities to the public by any existing holders of such specified securities in an unlisted issuer. In order to qualify as an Initial public offer, the issue shall be made to the public and not to the existing shareholders of the unlisted issuer company. (ii) Further public offer (FPO) or Follow on offer: means an offer of specified securities by a listed issuer to the public for subscription and includes an offer for sale of specified securities to the public by any existing holders of such specified securities in a listed issuer
Rights issue	Means an offer of specified securities by a listed issuer to the shareholders of the issuer as on the record date fixed for the said purpose, is called right issue.
Composite issue	When the issue of shares or convertible securities by a listed issuer on public cum-rights basis, wherein the allotment in both public issue and rights issue is proposed to be made simultaneously is called composite issue.

¹ a company or a body corporate authorized to issue specified securities under the relevant laws and whose specified securities are being issued and/or offered for sale in accordance with these regulations;

Bonus issue	When an issuer makes an issue of shares to its existing shareholders without any consideration based on the number of shares already held by them as on a record date it is called a bonus issue. The shares are issued out of the Company's free reserve or share premium account in a particular ratio to the number of securities held on a record date.
Private placement	When an issuer makes an issue of shares or convertible securities to a select group of persons not exceeding 50 or such higher number as may be prescribed which is 200 persons in the aggregate in a financial year. It is neither a rights issue nor a public issue, it is called a private placement. Private placement of shares or convertible securities by listed issuer can be of two types: (i) Preferential issue: means an issue of specified securities by a listed issuer to any select person or group of persons on a private placement basis in accordance with Chapter V of these regulations and does not include an offer of specified securities made through employee stock option scheme, employee stock purchase scheme or an issue of sweat equity shares or depository receipts issued in a country outside India or foreign securities; The issuer is required to comply with various provisions which inter-alia include pricing, disclosures in the notice, lock-in etc., in addition to the requirements specified in the Companies Act. (ii) Qualified Institutions placement (QIP): means issue of eligible securities by a listed issuer to qualified institutional buyers on a private placement basis and includes an offer for sale of specified securities by the promoters and/or promoter group on a private placement basis, in terms of these regulations.

OTHER RELEVANT DEFINITIONS (REGULATION 2)

"Book building" means a process undertaken to elicit demand and to assess the price for determination of the quantum or value or coupon of specified securities or Indian Depository Receipts, as the case may be, in accordance with these regulations; [Regulation 2(1)(g)]

Basically, book building is the process by which an underwriter attempts to determine the price at which an public issue will be offered.

"Convertible debt instrument" means an instrument which creates or acknowledges indebtedness and is convertible into equity shares of the issuer at a later date at or without the option of the holder of the instrument, whether constituting a charge on the assets of the issuer or not; [Regulation 2(1)(j)]

"Convertible security" means a security which is convertible into or exchangeable with equity shares of the issuer at a later date, with or without the option of the holder of such security and includes convertible debt instrument and convertible preference shares; [Regulation 2(1)(k)]

"Designated stock exchange" means a recognised stock exchange having nationwide trading terminals chosen by the issuer on which securities of an issuer are listed or proposed to be listed for the purpose of a particular issue of specified securities under these regulations:

Provided that, the issuer may choose a different recognised stock exchange as a designated stock exchange for any subsequent issue of specified securities; [Regulation 2(1)(l)]

"Green shoe option" means an option of allotting equity shares in excess of the equity shares offered in the public issue as a post-listing price stabilizing mechanism; [Regulation 2(1)(s)]

It can be understood in layman language as an over-allotment option. It is a price stabilization mechanism which is used in case of listing of Initial Public offer (IPO) or further public offer within first 30 days from the day of listing. The intent is to provide price support in case prices falls below issue prices.

"Offer document" means a red herring prospectus, prospectus or shelf prospectus, as applicable, referred to under the Companies Act, 2013, in case of a public issue, and a letter of offer in case of a rights issue; [Regulation 2(1)(kk)]

APPLICABILITY OF THE REGULATIONS (REGULATION 3)

These regulations shall apply to the following:

(a) an initial public offer

- by an unlisted issuer;

(b) a rights issue

- by a listed issuer with aggregate value of the issue fifty crore rupees or more;

(c) a further public offer

- by a listed issuer;

(d) a preferential issue

- by a listed issuer;

(e) a qualified institutions placement

- by a listed issuer;

(f) an initial public offer

- of Indian depository receipts;

(g) a rights issue of

- Indian depository receipts;

(h) an initial public offer

- by a small and medium enterprise;

(i) a listing

- on the innovators growth platform through an issue or without an issue; and

(j) a bonus issue

- by a listed issuer;

However, in case of **rights issue of size less than fifty crore rupees**- the issuer shall prepare the letter of offer in accordance with requirements as specified in these regulations and file the same with the Board for information and dissemination on the Board's website.

Exception: These regulations shall not apply to issue of securities under clauses (b), (d) and (e) of sub-regulation (1) of regulation 9 of Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

INITIAL PUBLIC OFFER ON MAIN BOARD

Eligibility Requirements [Regulation 4-8A]

1. Reference date (Regulation 4): An issuer making an initial public offer of specified securities shall satisfy the conditions of this Chapter as on the date of filing of the draft offer document with the Board and also as on the date of filing the offer document with the Registrar of Companies.

2. Entities not eligible to make an initial public offer (Regulation 5): Under following circumstances—

- (1) An issuer shall not be eligible to make an initial public offer—
 - (a) If the issuer, any of its promoters, promoter group or directors or selling shareholders are **debarred from accessing the capital market** by the Board.
 - (b) If any of the promoters or directors of the issuer **is a promoter or director of any other company which is debarred** from accessing the capital market by the Board.
 - (c) If the issuer or any of its promoters or directors is a **wilful defaulter or a fraudulent borrower**.
 - (d) If any of its promoters or directors is a **fugitive economic offender**.

Explanation—The restrictions under clauses (a) and (b) above, shall not apply to the persons or entities mentioned therein, **who were debarred in the past by the Board and the period of debarment is already over** as on the date of filing of the draft offer document with the Board.

- (2) An issuer shall not be eligible to make an initial public offer **if there are any outstanding convertible securities or any other right which would entitle any person with any option to receive equity shares of the issuer:**

Exception: the provisions of this sub-regulation (2) shall not apply to:

- (a) **outstanding options granted to employees:** Whether such an employee is currently an employee or not, pursuant to an employee stock option scheme in compliance with the Companies Act, 2013, the relevant Guidance Note or accounting standards, if any, issued by the Institute of Chartered Accountants of India or pursuant to the Companies Act, 2013, in this regard;
- (b) **fully paid-up outstanding convertible securities:** Such securities which are required to be converted on or before the date of filing of the red herring prospectus (in case of book-built issues) or the prospectus (in case of fixed price issues), as the case may be.

3. Eligibility requirements for an initial public offer (Regulation 6)

- (1) An issuer shall be eligible to make an initial public offer only if:

- (a) it has **net tangible assets of at least three crore rupees**, calculated on a restated and consolidated basis, 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 utilised or made firm commitments to utilise 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 initial public offer is made entirely through an offer for sale;
- (b) it has an **average operating profit of at least fifteen crore rupees**, calculated on a restated and consolidated basis, during the preceding three years (of twelve months each), with operating profit in each of these preceding three years;
- (c) it has a **net worth of at least one crore rupees** in each of the preceding three full years (of twelve months each), calculated on a restated and consolidated basis
- (d) if it has **changed its name** within the last one year, **at least fifty per cent of the revenue**, calculated on a restated and consolidated basis, for the preceding one full year has been earned by it from the activity indicated by its new name.
- (2) **Exception to the above in sub-regulation (1):** An issuer not satisfying the condition stipulated in sub-regulation (1) shall be eligible to make an initial public offer only if it fulfils the following conditions:
- the issue is made through the book-building process; and
 - the issuer undertakes to allot at least seventy five per cent of the net offer to qualified institutional buyers; and
 - to refund the full subscription money if it fails to do so.
- (3) **If an issuer has issued ²SR equity shares** to its promoters/founders, the said issuer shall be allowed to do an initial public offer of only ordinary shares for listing on the Main Board subject to compliance with the provisions of this Chapter and these clauses—
- (i) the **issuer shall be intensive in the use of technology, information technology, intellectual property, data analytics, bio-technology or nano-technology** to provide products, services or business platforms with substantial value addition;
 - (ii) **the net worth** of the SR shareholder, as determined by a Registered Valuer, shall **not be more than rupees one thousand crore**.

² means the equity shares of an issuer having superior voting rights compared to all other equity shares issued by that issuer

Explanation—While determining the individual net worth of the SR shareholder, his investment/shareholding in other listed companies shall be considered but not that of his shareholding in the issuer company;

- (iii) the **SR shares were issued only to the promoters/founders** who hold an executive position in the issuer company;
- (iv) the **issue of SR equity shares had been authorized by a special resolution** passed at a general meeting of the shareholders of the issuer, where the notice calling for such general meeting specifically provided for—
 - (a) the size of issue of SR equity shares;
 - (b) ratio of voting rights of SR equity shares vis-à-vis the ordinary shares;
 - (c) rights as to differential dividends, if any;
 - (d) sunset provisions, which provide for a time frame for the validity of such SR equity shares;
 - (e) matters in respect of which the SR equity shares would have the same voting right as that of the ordinary shares;
- (v) the SR equity shares have been issued **prior to the filing of draft red herring prospectus** and held for a period of at least three months prior to the filing of the red herring prospectus;
- (vi) the SR equity shares shall have **voting rights** in the ratio of a minimum of 2:1 upto a maximum of 10:1 compared to ordinary shares and such ratio shall be in whole numbers only;
- (vii) the SR equity shares shall have the **same face value** as the ordinary shares;
- (viii) the issuer **shall only have one class** of SR equity shares;
- (ix) the SR equity shares **shall be equivalent to ordinary equity shares** in all respects, except for having superior voting rights.

4. General conditions (Regulation 7)

- (1) An issuer making an initial public offer shall ensure that:
 - (a) **It has made an application to one or more stock exchanges:** This is done with an intent to seek an in-principle approval for listing of its specified securities on such stock exchanges and has chosen one of them as the designated stock exchange, in terms of Schedule XIX;
 - (b) **Entered into an agreement with a depository** for dematerialisation of the specified securities already issued and proposed to be issued;

- (c) All its **specified securities held by the promoters are in dematerialised form** prior to filing of the offer document;
 - (d) All its **existing partly paid-up equity shares have either been fully paid-up or have been forfeited**;
 - (e) It has **made firm arrangements of finance** through verifiable means towards seventy five per cent of the stated means of finance for a specific project proposed to be funded from the issue proceeds, excluding the amount to be raised through the proposed public issue or through existing identifiable internal accruals.
- (2) The **amount for general corporate purposes**, as mentioned in objects of the issue in the draft offer document and the offer document **shall not exceed twenty five per cent of the amount being raised by the issuer**.

Where an issuer had been a partnership firm or a limited liability partnership: As per explanation (II), the track record of operating profit of the partnership firm or the limited liability partnership shall be considered only if the financial statements of the partnership business for the period during which the issuer was a partnership firm or a limited liability partnership, conform to and are revised in the format prescribed for companies under the Companies Act, 2013 and also comply with the following:

- (a) **Adequate disclosures** are made in the financial statements as required to be made by the issuer as per Schedule III of the Companies Act, 2013;
- (b) the **financial statements are duly certified by the statutory auditor** stating that:
 - (i) the accounts and the disclosures made are in accordance with the provisions of Schedule III of the Companies Act, 2013;
 - (ii) the applicable accounting standards have been followed;
 - (iii) the financial statements present a true and fair view of the firm's accounts;

In case of an issuer formed out of a division of an existing company, Explanation (III) states that the track record of distributable profits of the division spun-off shall be considered only if the requirements regarding financial statements as provided for partnership firms or limited liability partnerships in Explanation (II) are complied with.

- (3) **Ceiling on the amount raised by the issuer:** The amount for:
- (i) general corporate purposes, and
 - (ii) such objects where the issuer company has not identified acquisition or investment target, as mentioned in objects of the issue in the draft offer document and the offer document, shall **not exceed thirty five per cent of the amount being raised by the issuer**.

Provided that the **amount raised for such objects where the issuer company has not identified acquisition or investment target**, as mentioned in objects of the issue in the draft offer document and the offer document, shall not exceed twenty five per cent of the amount being raised by the issuer:

Provided further that such limits shall not apply if the proposed acquisition or strategic investment object has been identified and suitable specific disclosures about such acquisitions or investments are made in the draft offer document and the offer document at the time of filing of offer documents.

5. Additional conditions for an offer for sale: Only such **fully paid-up equity shares** may be offered for sale to the public, which have been **held by the sellers for a period of at least one year prior to the filing of the draft offer document**:

In case where shares received on conversion : **Provided** that in case the equity shares received on conversion or exchange of fully paid-up compulsorily convertible securities including depository receipts are being offered for sale, the holding period of such convertible securities, including depository receipts, as well as that of resultant equity shares together shall be considered for the purpose of calculation of one year period referred in this sub-regulation:

Provided further that such holding period of one year shall be required to be complied with at the time of filing of the draft offer document.

Explanation—If the equity shares arising out of the conversion or exchange of the fully paid-up compulsorily convertible securities are being offered for sale, the conversion or exchange should be completed prior to filing of the offer document (i.e. red herring prospectus in the case of a book built issue and prospectus in the case of a fixed price issue), provided full disclosures of the terms of conversion or exchange are made in the draft offer document:

When requirement of holding equity shares for a period of one year shall not apply?

- (a) in case of **an offer for sale of a Government company or statutory authority or corporation or any special purpose vehicle** set up and controlled by any one or more of them, which is engaged in the infrastructure sector;
- (b) if the **equity shares offered for sale were acquired pursuant to any scheme approved by a High Court or approved by a Tribunal or the Central Government** under the sections 230 to 234 of Companies Act, 2013, as applicable, in lieu of business and invested capital which had been in existence for a period of more than one year prior to approval of such scheme;
- (c) if the **equity shares offered for sale were issued under a bonus issue** on securities held for a period of at least one year prior to the filing of the draft offer document with the Board and further subject to the following:

- (i) such **specified securities** being issued out of **free reserves and share premium** existing in the books of account as at the end of the financial year preceding the financial year in which the draft offer document is filed with the Board; and
- (ii) such **equity shares not being issued by utilisation of revaluation reserves or unrealized profits** of the issuer.

6. Additional conditions for an offer for sale for issues under sub-regulation (2) of regulation 6 (Regulation 8A)

For issues where draft offer document is filed under sub-regulation (2) of regulation 6 of these regulations:

- (a) **shares offered for sale to the public by shareholder(s) holding**, individually or with persons acting in concert, **more than twenty per cent of pre-issue shareholding** of the issuer based on fully diluted basis, shall not exceed more than fifty per cent of their pre-issue shareholding on fully diluted basis;
- (b) **shares offered for sale to the public by shareholder(s) holding**, individually or with persons acting in concert, **less than twenty per cent of pre-issue shareholding** of the issuer based on fully diluted basis, shall not exceed more than ten per cent of pre-issue shareholding of the issuer on fully diluted basis;
- (c) **for shareholder(s) holding**, individually or with persons acting in concert, **more than twenty per cent of pre-issue shareholding of the issuer based on fully diluted basis**, provisions of **lock-in** as specified under regulation 17 of these regulations shall be applicable, and relaxation from lock-in as provided under clause (c) of regulation 17 of these regulations shall not be applicable

ISSUE OF CONVERTIBLE DEBT INSTRUMENTS AND WARRANTS

1. Eligibility requirements for issue of convertible debt instruments (Regulation 9)

An issuer shall be eligible to make an initial public offer of convertible debt instruments even without making a prior public issue of its equity shares and listing thereof.

Provided that it is not in default of payment of interest or repayment of principal amount in respect of debt instruments issued by it to the public, if any, for a period of more than six months.

2. Additional requirements for issue of convertible debt instruments (Regulation 10)

- (1) In addition to other requirements laid down in these regulations, an issuer making an initial public offer of convertible debt instruments shall also comply with the **following conditions**:
 - (a) it has **obtained credit rating** from at least one credit rating agency;
 - (b) it has **appointed at least one debenture trustee** in accordance with the provisions of the Companies Act, 2013 and the Securities and Exchange Board of India (Debenture Trustees) Regulations, 1993;

- (c) it shall **create a debenture redemption reserve** in accordance with the provisions of the Companies Act, 2013 and rules made thereunder;
- (d) if the issuer proposes **to create a charge or security on its assets** in respect of secured convertible debt instruments, it **shall ensure** that:
 - i **such assets are sufficient to discharge the principal amount** at all times;
 - ii **such assets are free from any encumbrance**;
 - iii where security is already created on such assets in favour of any existing lender or security trustee or the issue of convertible debt instruments is proposed to be secured by creation of security on a leasehold land, the **consent of such lender or security trustee or lessor for a second or pari passu charge has been obtained and submitted** to the debenture trustee before the opening of the issue;
 - iv the **security or asset cover shall be arrived at after reduction of the liabilities having a first or prior charge**, in case the convertible debt instruments are secured by a second or subsequent charge.
- (2) The issuer shall **redeem the convertible debt instruments in terms of the offer document**.

3. Conversion of optionally convertible debt instruments into equity shares (Regulation 11)

- (1) **Consent for conversion of any convertible debt instruments:** The issuer shall not convert its optionally convertible debt instruments into equity shares unless the holders of such convertible debt instruments have sent their positive consent to the issuer and non-receipt of reply to any notice sent by the issuer for this purpose shall not be construed as consent for conversion of any convertible debt instruments.
- (2) **When no option of not converting the convertible portion into equity shares is provided:** Where the value of the convertible portion of any listed convertible debt instruments issued by an issuer exceeds ten crore rupees and the issuer has not determined the conversion price of such convertible debt instruments at the time of making the issue, the holders of such convertible debt instruments shall be given the option of not converting the convertible portion into equity shares.

Provided that where the upper limit on the price of such convertible debt instruments and justification thereon is determined and disclosed to the investors at the time of making the issue, it shall not be necessary to give such option to the holders of the convertible debt instruments for converting the convertible portion into equity share capital within the said upper limit.
- (3) **Right of redeem to the issuer:** Where an option is to be given to the holders of the convertible debt instruments in terms of sub-regulation (2) and if one or more of such holders

do not exercise the option to convert the instruments into equity share capital at a price determined in the general meeting of the shareholders, the issuer shall redeem that part of the instruments within one month from the last date by which option is to be exercised, at a price which shall not be less than its face value.

- (4) The provision of **sub-regulation (2)** shall not apply if such redemption is as per the disclosures made in the offer document.

4. Issue of convertible debt instruments for financing (Regulation 12)

An issuer **shall not issue convertible debt instruments for financing or for providing loans** to or for acquiring shares of any person who is part of the promoter group or group companies:

Provided that an issuer shall be eligible to issue fully convertible debt instruments for these purposes if the period of conversion of such debt instruments is less than eighteen months from the date of issue of such debt instruments.

5. Issue of warrants (Regulation 13)

An issuer shall be eligible to issue warrants in an initial public offer subject to the following:

- (a) the **tenure of such warrants shall not exceed eighteen months** from the date of their allotment in the initial public offer;
- (b) a **specified security** may have one or more warrants attached to it;
- (c) the **price or formula for determination of exercise price of the warrants shall be determined** upfront and disclosed in the offer document and at least twenty-five per cent. of the consideration amount based on the exercise price shall also be received upfront;

Provided that in case the exercise price of warrants is based on a formula, twenty-five per cent. consideration amount based on the cap price of the price band determined for the linked equity shares or convertible securities shall be received upfront.

- (d) in case the **warrant holder does not exercise the option** to take equity shares against any of the warrants held by the warrant holder, **within three months** from the date of payment of consideration, such consideration made in respect of such warrants shall be forfeited by the issuer.

PROMOTERS' CONTRIBUTION

1. Minimum promoters' contribution (Regulation 14)

- (1) The promoters of the issuer shall hold at least **twenty per cent of the post-issue capital**:

Provided that in case the post-issue shareholding of the promoters is less than twenty per cent, **alternative investment funds or foreign venture capital investors or scheduled commercial banks or public financial institutions or insurance companies** registered with Insurance Regulatory and Development Authority of India, **may contribute to meet the**

shortfall in minimum contribution as specified for the promoters, **subject to a maximum of ten per cent of the post-issue capital without being identified as promoter(s):**

When requirement of minimum promoters' contribution shall not apply?

The requirement of minimum promoters' contribution shall not apply in case an issuer does not have any identifiable promoter.

(2) The **minimum promoters' contribution** shall be as follows:

(a) the **promoters shall contribute twenty per cent** as stipulated in sub-regulation (1), as the case may be, either by way of equity shares including SR equity shares held, if any, or by way of subscription to convertible securities:

Provided that if the **price of the equity shares allotted pursuant to conversion is not pre-determined and not disclosed** in the offer document- the promoters shall contribute only by way of subscription to the convertible securities being issued in the public issue and shall undertake in writing to subscribe to the equity shares pursuant to conversion of such securities.

(b) in case of **any issue of convertible securities which are convertible or exchangeable on different dates** and if the promoters' contribution is by way of equity shares (conversion price being pre-determined), such contribution shall not be at a price lower than the weighted average price of the equity share capital arising out of conversion of such securities.

(c) subject to the provisions of clauses (a) and (b) above, **in case of an initial public offer of convertible debt instruments without a prior public issue of equity shares**, the promoters shall bring in a contribution of at least twenty per cent of the project cost in the form of equity shares, subject to contributing at least twenty per cent of the ³issue size from their own funds in the form of equity shares:

Provided that if the **project is to be implemented in stages**, the promoters' contribution shall be with respect to total equity participation till the respective stage *vis-à-vis* the debt raised or proposed to be raised through the public issue.

(3) The **promoters shall satisfy the requirements of this regulation** at least one day prior to the date of opening of the issue.

(4) In case the **promoters have to subscribe** to equity shares or convertible securities **towards minimum promoters' contribution**, the amount of promoters' contribution shall be kept in an escrow account with a scheduled commercial bank, which shall be released to the issuer along with the release of the issue proceeds:

³ "issue size" includes offer through offer document and promoters' contribution brought in as part of the issue;

Provided that where the promoters' contribution has already been brought in and utilised, the issuer shall give the cash flow statement disclosing the use of such funds in the offer document:

Where the minimum promoters' contribution is more than one hundred crore rupees and the initial public offer is for partly paid shares, there the promoters shall bring in at least one hundred crore rupees before the date of opening of the issue and the remaining amount may be brought on a *pro rata* basis before the calls are made to the public.

Explanation—For the purpose of this regulation:

- (I) Promoters' contribution shall be computed on the basis of the post-issue expanded capital:
 - (a) assuming full proposed conversion of convertible securities into equity shares;
 - (b) assuming exercise of all vested options, where any employee stock options are outstanding at the time of initial public offer in terms of proviso (a) to sub-regulation (2) of regulation 5.
- (II) For computation of "weighted average price":
 - (a) "weight" means the number of equity shares arising out of conversion of such specified securities into equity shares at various stages;
 - (b) "price" means the price of equity shares on conversion arrived at after taking into account the pre-determined conversion price at various stages.

LOCK-IN AND RESTRICTIONS ON TRANSFERABILITY

1. Lock-in of specified securities held by the promoters (Regulation 16)

- (1) **Specified securities are not transferable:** The specified securities held by the promoters shall not be transferable (hereinafter referred to as "lock-in") for the periods as stipulated hereunder:
 - (a) minimum promoters' contribution including contribution made by alternative investment funds or foreign venture capital investors or scheduled commercial banks or public financial institutions or insurance companies registered with Insurance Regulatory and Development Authority of India referred to in proviso to sub-regulation (1) of regulation 14- shall be locked-in for a period of **eighteen months from the date of allotment** in the initial public offer:

Provided that in case the **majority of the issue proceeds** excluding the portion of offer for sale **is proposed to be utilized for 'capital expenditure'**, then the lock-in period shall be three years from the date of allotment in the initial public offer;

- (b) **promoters' holding in excess of minimum promoters' contribution** shall be locked-in for a period of six months from the date of allotment in the initial public offer:

Provided that in case the **majority of the issue proceeds** excluding the portion of offer for sale **is proposed to be utilized for capital expenditure**, then the lock-in period shall be one year from the date of allotment in the initial public offer.

- (2) The **SR equity shares shall be under lock-in** until conversion into equity shares having voting rights same as that of ordinary shares or shall be locked-in for a period specified in sub-regulation (1), whichever is later.

2. **Lock-in of specified securities held by persons other than the promoters (Regulation 17)**

The **entire pre-issue capital** held by persons other than the promoters **shall be locked-in for a period of six months** from the date of allotment in the initial public offer.

However that nothing contained in this regulation shall apply to:

- (a) **equity shares allotted to employees.** Whether the person is currently an employee or not, under an employee stock option or employee stock purchase scheme of the issuer prior to the initial public offer, if the issuer has made full disclosures with respect to such options or scheme in accordance with Part A of Schedule VI;
- (b) **equity shares held by an employee stock option trust or transferred to the employees by an employee stock option trust** pursuant to exercise of options by the employees, whether currently employees or not, in accordance with the employee stock option plan or employee stock purchase scheme:

Provided that the equity shares allotted to the employees shall be subject to the provisions of lock-in as specified under the Securities and Exchange Board of India (Share Based Employee Benefits) Regulations, 2014.

- (c) **equity shares held by a venture capital fund or alternative investment fund of Category I or Category II or a foreign venture capital investor:**

Provided that such equity shares shall be locked in for a period of at least six months from the date of purchase by the venture capital fund or alternative investment fund of Category I or Category II or foreign venture capital investor.

⁴ "capital expenditure" shall include civil work, miscellaneous fixed assets, purchase of land, building and plant and machinery, etc

Explanation (i)—For the purpose of clause (c), **in case such equity shares have resulted pursuant to conversion of fully paid-up compulsorily convertible securities**, the holding period of such convertible securities as well as that of resultant equity shares together shall be considered for the purpose of calculation of six months period and convertible securities shall be deemed to be fully paid-up, if the entire consideration payable thereon has been paid and no further consideration is payable at the time of their conversion.

(ii) For the purpose of clause (c), **in case such equity shares have resulted pursuant to a bonus issue**, then the holding period of such equity shares against which the bonus issue is made as well as holding period of resultant bonus equity shares together shall be considered for the purpose of calculation of six months period, subject to the following:

- (a) that the bonus shares being issued out of free reserves and share premium existing in the books of account as at the end of the financial year preceding the financial year in which the draft offer document is filed with the Board; and
- (b) that the bonus shares not being issued by utilisation of revaluation reserves or unrealized profits of the issuer.

3. Lock-in of specified securities lent to stabilising agent under the green shoe option (Regulation 18)

The lock-in provisions shall not apply with respect to the **specified securities lent to stabilising agent for the purpose of green shoe option**, during the period starting from the date of lending of such specified securities and ending on the date on which they are returned to the lender in terms of sub-regulation (5) or (6) of regulation 57:

Provided that the specified securities shall be locked-in for the remaining period from the date on which they are returned to the lender.

4. Lock-in of Partly-paid securities (Regulation 19)

If the **specified securities which are subject to lock-in are partly paid-up** and the amount called-up on such specified securities is less than the amount called-up on the specified securities issued to the public, the lock-in shall end only on the expiry of three years after such specified securities have become *pari passu* with the specified securities issued to the public.

5. Inscription or recording of non-transferability (Regulation 20)

The **certificates of specified securities which are subject to lock-in shall contain the inscription “non-transferable”** and specify the lock-in period and in case such specified securities are dematerialised, the issuer shall ensure that the lock-in is recorded by the depository.

6. Pledge of locked-in specified securities (Regulation 21)

Specified securities, except SR equity shares, held by the promoters and locked-in may be pledged as a collateral security for a loan. It is granted by a scheduled commercial bank or a

public financial institution or a systemically important non-banking finance company or a housing finance company, subject to the following:

- **if the specified securities are locked-in in terms of clause (a) of regulation 16**, in that case it is considered that the loan has been granted to the issuer company or its subsidiary(ies) for the purpose of financing one or more of the objects of the issue and pledge of specified securities is one of the terms of sanction of the loan;
- **if the specified securities are locked-in in terms of clause (b) of regulation 16 then it may be** the pledge of specified securities which is one of the terms of sanction of the loan.

Provided that such lock-in shall continue pursuant to the invocation of the pledge and such transferee shall not be eligible to transfer the specified securities till the lock-in period stipulated in these regulations has expired.

Transferability of locked-in specified securities (Regulation 22)

Subject to the provisions of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, **the specified securities**, except SR equity shares, **held by**

- (i) **the promoters and locked-in** as per regulation 16, **may be transferred** to another promoter or any person of the promoter group or a new promoter, and
- (ii) **the specified securities held by persons other than the promoters and locked-in** as per regulation 17, **may be transferred** to any other person holding the specified securities which are locked-in along with the securities proposed to be transferred:

Provided that the lock-in on such specified securities shall continue for the remaining period with the transferee and such transferee shall not be eligible to transfer them till the lock-in period stipulated in these regulations has expired.

DISCLOSURES IN AND FILING OF OFFER DOCUMENTS

1. Disclosures in the draft offer document and offer document (Regulation 24)

- (1) The ⁵draft offer document and ⁶offer document shall **contain all material disclosures** which are true and adequate to enable the applicants to take an informed investment decision.
- (2) the **red-herring prospectus, and prospectus** shall contain:
 - (a) disclosures specified in the Companies Act, 2013 and;
 - (b) disclosures specified in Part A of Schedule VI

⁵ draft offer document" means the draft offer document filed with the Board in relation to a public issue under these regulations;

⁶ offer document" means a red herring prospectus, prospectus or shelf prospectus, as applicable, referred to under the Companies Act, 2013, in case of a public issue, and a letter of offer in case of a rights issue

- (3) The lead manager(s) shall **exercise due diligence and satisfy themselves** about all aspects of the issue including the veracity and adequacy of disclosure in the draft offer document and the offer document.
- (4) The lead manager(s) shall **call upon the issuer, its promoters and its directors or in case of an offer for sale, also the selling shareholders, to fulfil their obligations as disclosed by them** in the draft offer document and the offer document and as required in terms of these regulations.
- (5) The lead manager(s) shall ensure that the **information contained** in the draft offer document and offer document and the particulars as per restated audited financial statements in the offer document **are not more than six months old** from the issue opening date.

2. Filing of the draft offer document and offer document (Regulation 25)

- (1) Prior to making an initial public offer, the **issuer shall file three copies of the draft offer document with the Board**, in accordance with Schedule IV, along with fees as specified in Schedule III, through the lead manager(s).
- (2) The lead manager(s) shall submit the following certifications to the Board along with the draft offer document:
 - (a) a certificate, confirming that an agreement has been entered into between the issuer and the lead manager(s);
 - (b) a due diligence certificate as per Form A of Schedule V;
 - (c) in case of an issue of convertible debt instruments, a due diligence certificate from the debenture trustee as per Form B of Schedule V;
- (3) The **issuer shall also file the draft offer document with the stock exchange(s) where the specified securities are proposed to be listed**, and submit to the stock exchange(s), the Permanent Account Number, bank account number and passport number of its promoters where they are individuals, and Permanent Account Number, bank account number, company registration number or equivalent and the address of the Registrar of Companies with which the promoter is registered, where the promoter is a body corporate.
- (4) The **Board may specify changes or issue observations**, if any, on the draft offer document within thirty days from the later of the following dates:
- (5) If the Board specifies any changes or issues observations on the draft offer document, **the issuer and lead manager(s) shall carry out such changes** in the draft offer document and shall submit to the Board an updated draft offer document complying with the observations issued by the Board and highlighting all changes made in the draft offer document and before filing the offer documents with the Registrar of Companies or an appropriate authority, as applicable.
 - (a) the date of **receipt of the draft offer document** under sub-regulation (1); or

- (b) the date of **receipt of satisfactory reply from the lead manager(s)**, where the Board has sought any clarification or additional information from them; or
 - (c) the date of **receipt of clarification or information from any regulator or agency**, where the Board has sought any clarification or information from such regulator or agency; or
 - (d) the date of receipt of a copy of in-principle approval letter issued by the stock exchange(s).
- (6) If there are any changes in the draft offer document in relation to the matters specified in Schedule XVI, **an updated offer document or a fresh draft offer document**, as the case may be, **shall be filed** with the Board along with fees specified in Schedule III.
- (7) **Copy of the offer documents shall also be filed** with the Board and the stock exchange(s) through the lead manager(s) promptly after filing the offer documents with Registrar of Companies.
- (8) The draft offer document and the offer document shall also be furnished to the Board in a **soft copy**.
- (9) The **lead manager(s) shall submit the following documents to the Board after issuance of observations** by the Board or after expiry of the period stipulated in sub-regulation (4) of regulation 25 if the Board has not issued observations:
- (a) a **statement certifying that all changes, suggestions and observations** made by the Board have been **incorporated** in the offer document;
 - (b) a **due diligence certificate as per Form C** of Schedule V, at the time of filing of the offer document;
 - (c) a **copy of the resolution passed** by the Board of directors of the issuer for allotting specified securities to promoter(s) towards amount received against promoters' contribution, before opening of the issue;
 - (d) a **certificate from a statutory auditor**, before opening of the issue, certifying that promoters' contribution has been received in accordance with these regulations, accompanying therewith the names and addresses of the promoters who have contributed to the promoters' contribution and the amount paid and credited to the issuer's bank account by each of them towards such contribution;
 - (e) a **due diligence certificate as per Form D** of Schedule V, in the event the issuer has made a disclosure of any material development by issuing a public notice pursuant to para 4 of Schedule IX.

3. Draft offer document and offer document to be available to the public(Regulation 26)

- (1) The draft offer document filed with the Board shall be made public for comments, if any, for a period of at least twenty one days from the date of filing, by hosting it on the websites of the Board,

stock exchanges where specified securities are proposed to be listed and lead manager(s) associated with the issue.

- (2) The issuer shall, within two days of filing the draft offer document with the Board, make a public announcement in one English national daily newspaper with wide circulation, one Hindi national daily newspaper with wide circulation and one regional language newspaper with wide circulation at the place where the registered office of the issuer is situated, disclosing the fact of filing of the draft offer document with the Board and inviting the public to provide their comments to the Board, the issuer or the lead manager(s) in respect of the disclosures made in the draft offer document.
- (3) The lead manager(s) shall, after expiry of the period stipulated in sub-regulation (1), file with the Board, details of the comments received by them or the issuer from the public, on the draft offer document, during that period and the consequential changes, if any, that are required to be made in the draft offer document.
- (4) The issuer and the lead manager(s) shall ensure that the offer documents are hosted on the websites as required under these regulations and its contents are the same as the versions as filed with the Registrar of Companies, Board and the stock exchanges, as applicable.
- (5) The lead manager(s) and the stock exchanges shall provide copies of the offer document to the public as and when requested and may charge a reasonable sum for providing a copy of the same.

PRICING

Pricing: The issuer may determine the price of equity shares, and in case of convertible securities, the coupon rate and the conversion price, in consultation with the lead manager(s)/through the book building process as the case may be.

Price and Price Band:

- (1) **The issuer may mention a price or a price band in the offer document** (in case of a fixed price issue) and **a floor price or a price band in the red herring prospectus** (in case of a book built issue) and determine the price at a later date before filing the prospectus with the Registrar of Companies:

Provided that the prospectus filed with the Registrar of Companies shall contain only one price or the specific coupon rate, as the case may be.
- (2) The **cap on the price band**, and the coupon rate in case of convertible debt instruments, shall be less than or equal to one hundred and twenty per cent of the floor price:

Provided that the cap of the price band shall be at least one hundred and five per cent of the floor price.
- (3) The **floor price or the final price shall not be less than the face value of the specified securities**.

- (4) Where the **issuer opts not to make the disclosure of the floor price or price band** in the red herring prospectus, the issuer shall announce the floor price or the price band at least two working days before the opening of the issue in the same newspapers in which the pre-issue advertisement was released or together with the pre-issue advertisement in the format prescribed under Part A of Schedule X.
- (5) The announcement referred to in sub-regulation (4) shall contain **relevant financial ratios computed for both upper and lower end of the price band** and also a statement drawing attention of the investors to the section titled "basis of issue price" of the offer document.
- (6) The **announcement** referred to in sub-regulation (4) **and the relevant financial ratios** referred to in sub-regulation (5) shall **be disclosed on the websites of the stock exchange(s)** and shall also be pre-filled in the application forms to be made available on the websites of the stock exchange(s).

Differential pricing (Regulation 30):

- (1) The **issuer may offer its specified securities at different prices**, subject to the following:
 - (a) retail individual investors or retail individual shareholders or employees entitled for reservation made under regulation 33 may be offered specified securities at a price not lower than by more than ten per cent. of the price at which net offer is made to other categories of applicants, excluding anchor investors;
 - (b) in case of a book built issue, the price of the specified securities offered to the anchor investors shall not be lower than the price offered to other applicants;
 - (c) In case the issuer opts for the alternate method of book building in terms of Part D of Schedule XIII, the issuer may offer the specified securities to its employees at a price not lower than by more than ten per cent. of the floor price.
- (2) **Discount**, if any, shall be expressed in rupee terms in the offer document.

ISSUANCE CONDITIONS AND PROCEDURE

Opening of the issue (Regulation 44)

- (1) **Time period for opening of public issue:** Subject to the compliance with the provisions of the Companies Act, 2013, a public issue may be opened **within twelve months** from the date of issuance of the observations by the Board under regulation 25;
- (2) **In case of prospectus and red hearing prospectus:** An issue shall be opened after at least three working days from the date of filing, the red herring prospectus, in case of a book built issue and the prospectus, in case of a fixed price issue, with the Registrar of Companies.

Minimum subscription (Regulation 45)

- (1) The **minimum subscription** to be received in the issue shall be at least **ninety per cent of the offer** through the offer document, except in case of an offer for sale of specified securities:

Provided that the minimum subscription to be received shall be subject to the allotment of minimum number of specified securities, as prescribed under the Securities Contracts (Regulation) Rules, 1957.

- (2) In the event of **non-receipt of minimum subscription**, all **application monies received shall be refunded** to the applicants forthwith, but not later than four days from the closure of the issue.

Period of subscription (Regulation 46)

- (1) An **initial public offer shall be kept open for at least three working days and not more than ten working days**.
- (2) In case of a **revision in the price band**: The issuer shall extend the bidding (issue) period disclosed in the red herring prospectus, for a **minimum period of three working days**, subject to the provisions of sub-regulation (1).
- (3) In case of **force majeure, banking strike or similar circumstances**: The issuer may, for reasons to be recorded in writing, extend the bidding (issue) period disclosed in the red herring prospectus (in case of a book built issue) or the issue period disclosed in the prospectus (in case of a fixed price issue), for a minimum period of three working days, subject to the provisions of sub-regulation (1).

Application and minimum application value (Regulation 47)

- The issuer shall stipulate in the offer document the minimum application size in terms of number of specified securities which shall fall within the range of ⁷ minimum application value of ten thousand rupees to fifteen thousand rupees.
- The issuer shall invite applications in multiples of the minimum application value.
- The minimum sum payable on application per specified security shall be at least twenty five per cent. of the issue price:
- Provided that in case of an offer for sale, the full issue price for each specified security shall be payable at the time of application.

Manner of calls (Regulation 48)

If the issuer **proposes to receive subscription monies in calls**, it shall ensure that the outstanding subscription money is called within twelve months from the date of allotment in the issue.

⁷ minimum application value" shall be with reference to the issue price of the specified securities and not with reference to the amount payable on application.

If any applicant fails to pay the call money within the said twelve months, the equity shares on which there are calls in arrears along with the subscription money already paid on such shares, shall be forfeited:

Exemption: it shall not be necessary to call the outstanding subscription money within twelve months, if the issuer has appointed a monitoring agency in terms of regulation 41.

Allotment procedure and basis of allotment (Regulation 49)

- (1) **When no allotment shall be made:** The issuer shall not make an allotment pursuant to a public issue if the number of prospective allottees is less than one thousand.
- (2) **Limit on allotment of the specified securities:** the issuer shall not make any allotment in excess of the specified securities offered through the offer document except in case of oversubscription for the purpose of rounding off to make allotment, in consultation with the designated stock exchange:

Provided that in case of oversubscription, an allotment of not more than one per cent of the net offer to public may be made for the purpose of making allotment in minimum lots.

- (3) **Allotment to applicants:** The allotment of specified securities to applicants (other than to the retail individual investors non-institutional investors and anchor investors) shall be on a proportionate basis within the respective investor categories and the number of securities allotted shall be rounded off to the nearest integer, subject to minimum allotment being equal to the minimum application size as determined and disclosed in the offer document:

Provided that the value of specified securities allotted to any person, except in case of employees, in pursuance of reservation made under clause (a) of sub-regulation (1) or clause (a) of sub-regulation (2) of regulation 33, shall not exceed two lakhs rupees for retail investors or up to five lakhs rupees for eligible employees.

- (4) **Limit on allotment:** The allotment of specified securities to each retail individual investor shall not be less than the minimum bid lot, subject to the availability of shares in retail individual investor category, and the remaining available shares, if any, shall be allotted on a proportionate basis.
- (4A) **Allotment to non-institutional investor:** The allotment of specified securities to each non-institutional investor shall not be less than the minimum application size, subject to the availability of shares in non-institutional investors' category, and the remaining shares, if any, shall be allotted on a proportionate basis in accordance with the conditions specified in this regard in Schedule XIII of these regulations.
- (5) **The authorised employees of the designated stock exchange**, along with the lead manager(s) and registrars to the issue, **ensure that the basis of allotment is finalised in a fair and proper manner** in accordance with the procedure as shall specified in Part A of Schedule XIV.

Allotment, refund and payment of interest (Regulation 50)

- (1) The issuer and lead manager(s) shall ensure that the specified securities are allotted and/or application monies are refunded or unblocked within such period as may be specified by the Board.
- (2) The lead manager(s) shall ensure that the allotment, credit of dematerialised securities and refund or unblocking of application monies, as may be applicable, are done electronically.
- (3) Where the **specified securities are not allotted** and/or application monies are not refunded or unblocked within the period stipulated in sub-regulation (1) above, **the issuer shall undertake to pay interest at the rate of fifteen per cent per annum to the investors** and within such time as disclosed in the offer document and the lead manager(s) shall ensure the same.

Post-issue advertisements (Regulation 51)

- (1) The lead manager(s) shall **ensure that an advertisement giving details** relating to subscription, basis of allotment, number, value and percentage of all applications including ASBA, number, value and percentage of successful allottees for all applications including ASBA, date of completion of despatch of refund orders, as applicable, or instructions to self-certified syndicate banks by the registrar, date of credit of specified securities and date of filing of listing application, etc. **is released within ten days from the date of completion of the various activities** in at least one English national daily newspaper with wide circulation, one Hindi national daily newspaper with wide circulation and one regional language daily newspaper with wide circulation at the place where registered office of the issuer is situated.
- (2) Details specified in sub regulation (1) shall also be placed on the websites of the stock exchange(s).

Release of subscription money (Regulation 53)

- (1) **The lead manager(s) shall confirm to the bankers** to the issue by way of copies of listing and trading approvals that all formalities in connection with the issue have been completed and that the banker is free to release the money to the issuer or release the money for refund in case of failure of the issue.
- (2) In case the **issuer fails to obtain listing or trading permission** from the stock exchanges where the specified securities were to be listed, **it shall refund through verifiable means the entire monies received within four days** of receipt of intimation from stock exchanges rejecting the application for listing of specified securities, and if any such money is not repaid within four days after the issuer becomes liable to repay it, the issuer and every director of the company who is an officer in default shall, on and from the expiry of the fourth day, be jointly and severally liable to repay that money with interest at the rate of fifteen per cent. per annum.

- (3) The lead manager(s) shall ensure that the monies received in respect of the issue are released to the issuer in compliance with the provisions of Section 40(3) of the Companies Act, 2013, as applicable.

Reporting of transactions of the promoters and promoter group (Regulation 54)

The issuer shall ensure that all transactions in securities by the promoter and promoter group between the date of filing of the draft offer document or offer document, as the case may be, and the date of closure of the issue shall be reported to the stock exchange(s), within twenty four hours of such transactions.

Post-issue reports (Regulation 54)

The lead manager(s) shall submit a final post-issue report as specified in **Part A of Schedule XVII**, along with a due diligence certificate as per the format specified in **Form F of Schedule V**, within seven days of the date of finalization of basis of allotment or within seven days of refund of money in case of failure of issue.

MISCELLANEOUS

Restriction on further capital issues (Regulation 56)

An issuer shall not make any further issue of specified securities in any manner whether by way of public issue, rights issue, preferential issue, qualified institutions placement, issue of bonus shares or otherwise, **except pursuant to an employee stock option scheme**, during the period between the date of filing the draft offer document and the listing of the specified securities offered through the offer document or refund of application monies, unless full disclosures regarding the total number of specified securities or amount proposed to be raised from such further issue are made in such draft offer document or offer document, as the case may be.

Price stabilisation through green shoe option (Regulation 57)

- (1) An issuer may provide a **green shoe option for stabilising the post listing price** of its specified securities, subject to the following:
- (a) the issuer has been authorized, **by a resolution passed in the general meeting** of shareholders approving the public issue, to allot specified securities to the stabilising agent, if required, on the expiry of the stabilisation period;
 - (b) the issuer has appointed a lead manager as a **stabilising agent**, who shall be responsible for the price stabilisation process;
 - (c) prior to filing the draft offer document, **the issuer and the stabilising agent have entered into an agreement**, stating all the terms and conditions relating to the green shoe option including fees charged and expenses to be incurred by the stabilising agent for discharging its responsibilities;

- (d) prior to filing the offer document, **the stabilising agent has entered into an agreement with the promoters or pre-issue shareholders or both for borrowing specified securities** from them in accordance with clause (g) of this sub-regulation, specifying therein the maximum number of specified securities that may be borrowed for the purpose of allotment or allocation of specified securities in excess of the issue size (hereinafter referred to as the “over- allotment”), which shall not be in excess of fifteen per cent. of the issue size;
 - (e) subject to clause (d), the lead manager, **in consultation with the stabilising agent, shall determine the amount of specified securities to be over-allotted** in the public issue;
 - (f) the **draft offer document and offer document shall contain all material disclosures** about the green shoe option specified in this regard in Part A of **Schedule VI**;
 - (g) in case of an initial public offer pre-issue shareholders and promoters and in case of a further public offer pre-issue shareholders **holding more than five per cent. specified securities and promoters, may lend specified securities** to the extent of the proposed over-allotment;
 - (h) the **specified securities borrowed shall be in dematerialised form** and allocation of these securities shall be made pro-rata to all successful applicants.
- (2) For the purpose of **stabilisation of post-listing price** of the specified securities, **the stabilising agent shall determine the relevant aspects** including the timing of buying such securities, quantity to be bought and the price at which such securities are to be bought from the market.
 - (3) **The stabilisation process shall be available for a period not exceeding thirty days** from the date on which trading permission is given by the stock exchanges in respect of the specified securities allotted in the public issue.
 - (4) The **stabilising agent shall open a special account**, distinct from the issue account, with a bank for crediting the monies received from the applicants against the over-allotment and a special account with a depository participant for crediting specified securities to be bought from the market during the stabilisation period out of the monies credited in the special bank account.
 - (5) The **specified securities bought from the market and credited in the special account** with the depository participant **shall be returned** to the promoters or pre-issue shareholders immediately, in any case not later than two working days after the end of the stabilization period.

- (6) On expiry of the stabilisation period, if the **stabilising agent has not been able to buy specified securities** from the market to the extent of such securities over-allotted, **the issuer shall allot specified securities at issue price in dematerialised form to the extent of the shortfall to the special account with the depository participant**, within five days of the closure of the stabilisation period and such specified securities shall be returned to the promoters or pre-issue shareholders by the stabilising agent in lieu of the specified securities borrowed from them and the account with the depository participant shall be closed thereafter.
- (7) The **issuer shall make a listing application** in respect of the further specified securities allotted under sub-regulation (6), **to all the stock exchanges** where the specified securities allotted in the public issue are listed and the provisions of Chapter V of these regulations shall not be applicable to such allotment.
- (8) The **stabilising agent shall remit the monies** with respect to the specified securities allotted under sub-regulation (6) to the issuer from the special bank account.
- (9) Any **monies left in the special bank account after remittance of monies** to the issuer under sub-regulation (8) and deduction of expenses incurred by the stabilising agent for the stabilisation process shall be transferred to the Investor Protection and Education Fund established by the Board and the special bank account shall be closed soon thereafter.
- (10) The stabilising agent shall **submit a report** to the stock exchange on a daily basis during the stabilisation period and a final report to the Board in the format specified in **Schedule XV**.
- (11) The **stabilising agent shall maintain a register** for a period of at least three years from the date of the end of the stabilisation period and such register shall contain the following particulars:
 - (a) The names of the promoters or pre-issue shareholders from whom the specified securities were borrowed and the number of specified securities borrowed from each of them;
 - (b) The price, date and time in respect of each transaction effected in the course of the stabilisation process; and
 - (c) The details of allotment made by the issuer on expiry of the stabilisation process.

Alteration of rights of holders of specified securities (Regulation 58)

The issuer **shall not alter the terms** including the terms of issue of specified securities which may adversely affect the interests of the holders of that specified securities, **except with the consent in writing of the holders** of not less than three-fourths of the specified securities of that class or with the sanction of a special resolution passed at a meeting of the holders of the specified securities of that class.

Post-listing exit opportunity for dissenting shareholders (Regulation 59)

The promoters, or shareholders in control of an issuer, **shall provide an exit offer to dissenting shareholders** as provided for in the Companies Act, 2013, **in case of change in objects or variation in the terms of contract** related to objects referred to in the offer document as per conditions and manner is provided in Schedule XX.

Provided that the exit offer shall not apply where there are neither any identifiable promoters nor any shareholders in control of the issuer.

FURTHER PUBLIC OFFER**Eligibility Requirements (Regulation 101 -105)****1. Reference date (Regulation 101)**

An issuer making a further public offer of specified securities shall satisfy the conditions of this Chapter as on the date of filing:

- of the draft offer document with the Board, and also
- the offer document with the Registrar of Companies.

2. Entities not eligible to make a further public offer (Regulation 102)

An issuer **shall not be eligible** to make a further public offer:

- (a) if the issuer, any of its promoters, promoter group or directors, selling shareholders are **debarred from accessing the capital market** by the Board;
- (b) if any of the **promoters or directors of the issuer is a promoter or director of any other company which is debarred** from accessing the capital market by the Board;
- (c) if the **issuer or any of its promoters or directors is a wilful defaulter or a fraudulent borrower**;
- (d) if any of its **promoters or directors is a fugitive economic offender**.

Explanation—The restrictions under (a) and (b) above shall not apply to the persons or entities mentioned therein, who were debarred in the past by the Board and the period of debarment is already over as on the date of filing of the draft offer document with the Board.

3. Eligibility requirements for further public offer (Regulation 103)

- (1) **When an issuer shall be eligible?** An issuer shall be eligible to make a further public offer, **if it has not changed its name in the last one year** period immediately preceding the date of filing the relevant offer document:

Where if, an issuer has changed its name in the last one year period immediately preceding the date of filing the relevant offer document, **such an issuer shall make further public offer if at**

least fifty per cent of the revenue for the preceding one full year has been earned by it from the activity indicated by its new name.

- (2) **Where an issuer fails to satisfy the stipulated condition** - In such case, an issuer, shall make a further public offer only if:
- the issue is made through the book building process, and
 - the issuer undertakes to allot at least seventy five per cent of the net offer to qualified institutional buyers, and
 - to refund full subscription money if it fails to make the said minimum allotment to qualified institutional buyers.

4. General conditions (Regulation 104)

- (1) An issuer making a further public offer **shall ensure** that—
- (a) it has **made an application** to one or more stock exchanges to seek an in-principle approval for listing of its specified securities on such stock exchanges and has chosen one of them as the designated stock exchange, in terms of Schedule XIX;
 - (b) it has **entered into an agreement with a depository** for dematerialisation of specified securities already issued and proposed to be issued;
 - (c) all its **existing partly paid-up equity shares have either been fully paid-up** or have been forfeited;
 - (d) it has made **firm arrangements of finance** through verifiable means towards seventy five per cent of the stated means of finance for the specific project proposed to be funded from the issue proceeds, excluding the amount to be raised through the proposed public issue or through existing identifiable internal accruals.

Explanation—For the purposes of this regulation "finance for the specific project" shall mean finance for capital expenditures only

- (2) The **amount for general corporate purposes**, as mentioned in objects of the issue in the draft offer document and the offer document, **shall not exceed twenty five per cent of the amount** being raised by the issuer.

Explanation—For the purposes of this regulation, "project" means the object for which monies are proposed to be raised to cover the objects of the issue.

- (3) The **amount** for:
- (i) general corporate purposes, and
 - (ii) such objects where the issuer company has not identified acquisition/investment target, as mentioned in objects of the issue in the draft offer document and the offer document,

shall not exceed thirty five per cent of the amount being raised by the issuer:

Provided that the amount raised for such objects where the issuer **company has not identified acquisition or investment target**, as mentioned in objects of the issue in the draft offer document and the offer document, shall not exceed twenty five per cent of the amount being raised by the issuer:

Provided further that such limits shall not apply **if the proposed acquisition or strategic investment object has been identified** and suitable specific disclosures about such acquisitions or investments are made in the draft offer document and the offer document at the time of filing of offer documents.

5. Additional conditions for an offer for sale (Regulation 105)

Only such fully paid-up equity shares may be offered for sale to public **which have been held by the selling shareholder(s) for a period of at least one year** prior to the filing of the draft offer document:

Provided that in case the equity shares received on conversion or exchange of fully paid-up compulsorily convertible securities including depository receipts are being offered for sale, the holding period of such convertible securities, including depository receipts, as well as that of resultant equity shares together shall be considered for the purpose of calculation of one year period referred in this sub-regulation:

Provided further that such holding period of one year shall be required to be complied with at the time of filing of the draft offer document.

Explanation—If the equity shares arising out of the conversion or exchange of the fully paid-up compulsorily convertible securities are being offered for sale, the conversion or exchange should be completed prior to filing of the offer document (*i.e.* red herring prospectus in the case of a book built issue and prospectus in the case of a fixed price issue), provided full disclosures of the terms of conversion or exchange are made in the draft offer document:

Provided further that the requirement of holding the equity shares for a period of one year shall not apply:

- (a) in case of **an offer for sale of a Government company or statutory authority or corporation or any special purpose vehicle set up** and controlled by any one or more of them, which is engaged in the infrastructure sector;
- (b) if the **equity shares offered for sale were acquired pursuant to any scheme approved by a High Court or approved by a tribunal or the Central Government** under sections 230 to 234 of the Companies Act, 2013, as applicable, in lieu of business and invested capital which had been in existence for a period of more than one year prior to approval of such scheme;

- (c) if the **equity shares offered for sale were issued under a bonus issue** on securities held for a period of at least one year prior to the filing of the draft offer document with the Board and further subject to the following:
- (i) such specified securities being issued out of free reserves and share premium existing in the books of account as at the end of the financial year preceding the financial year in which the draft offer document is filed with the Board; and
 - (ii) such equity shares not being issued by utilisation of revaluation reserves or unrealized profits of the issuer.

ISSUE OF CONVERTIBLE DEBT INSTRUMENTS AND WARRANTS

1. Eligibility of issuer to make FPO of convertible debt instruments

An issuer shall be eligible to make a further public offer of convertible debt instruments **if its equity shares are already listed**;

Provided that it is **not in default in payment of interest or repayment of principal amount** in respect of debt instruments issued by it to the public, if any, **for a period of more than six months**.

2. Additional requirements for issue of convertible debt instruments (Regulation 107)

- (1) In addition to other requirements laid down in these regulations, an issuer making a public issue of convertible debt instruments **shall also comply with the following conditions** :
- (a) it has **obtained credit rating** for such convertible debt instrument from one or more credit rating agencies;
 - (b) it has **appointed at least one debenture trustee** in accordance with the provisions of the Companies Act, 2013 and the Securities and Exchange Board of India (Debenture Trustees) Regulations, 1993;
 - (c) it **shall create a debenture redemption reserve** in accordance with the provisions of the Companies Act, 2013 and rules made thereunder;
 - (d) if the **issuer proposes to create a charge or security on its assets** in respect of secured convertible debt instruments, it shall ensure that:
 - (i) such assets are sufficient to discharge the principal amount at all times;
 - (ii) such assets are free from any encumbrance;
 - (iii) where security is already created on such assets in favour of public financial institutions or scheduled commercial banks or the issue of convertible debt instruments is proposed to be secured by creation of security on a leasehold land,

the consent of such public financial institution, scheduled commercial bank or lessor for a second or pari passu charge has been obtained and submitted to the debenture trustee before the opening of the issue;

- (iv) the security or asset cover shall be arrived at after reduction of the liabilities having a first or prior charge, in case the convertible debt instruments are secured by a second or subsequent charge.

- (2) The issuer shall **redeem the convertible debt instruments** in terms of the offer document.

3. Roll over of non-convertible portion of partly convertible debt instruments (Regulation 108)

- (1) The non-convertible portion of partly convertible debt instruments issued by a listed issuer, the value of which exceeds ten crore rupees, may be rolled over, subject to compliance with the provisions of the Companies Act, 2013 and the following conditions:

- (a) seventy-five per cent. of the holders (in value) of the convertible debt instruments of the issuer have, through a resolution, approved the rollover through postal ballot;
- (b) the issuer has, along with the notice for passing the resolution, sent to all holders of the convertible debt instruments, an auditors' certificate on the cash flow of the issuer and with comments on the liquidity position of the issuer;
- (c) the issuer has undertaken to redeem the non-convertible portion of the partly convertible debt instruments of all the holders of the convertible debt instruments who have not agreed to the resolution;
- (d) credit rating has been obtained from at least one credit rating agency registered with the Board within a period of one month prior to the due date of redemption and has been communicated to the holders of the convertible debt instruments, before the roll over.

- (2) The creation of fresh security and execution of fresh trust deed shall not be mandatory if the existing trust deed or the security documents provide for continuance of the security till redemption of secured convertible debt instruments:

Provided that the debenture trustee shall decide if the issuer is required to create fresh security and to execute fresh trust deed.

4. Conversion of optionally convertible debt instruments into equity share capital (Regulation 109)

- (1) The issuer shall not convert its optionally convertible debt instruments into equity shares unless the **holders of such convertible debt instruments have sent their positive consent to the issuer** and non-receipt of reply to any notice sent by the issuer for this purpose shall not be construed as consent for conversion of any convertible debt instruments.

- (2) Where the **value of the convertible portion** of any listed convertible debt instruments issued by an issuer **exceeds ten crore rupees** and the issuer has not determined the conversion price of such convertible debt instruments at the time of making the issue, **the holders of such convertible debt instruments shall be given the option of not converting the convertible portion into equity shares:**

Provided that where the upper limit or conversion formula on the price of such convertible debt instruments and justification thereon is determined and disclosed to the investors at the time of making the issue, it shall not be necessary to give such option to the holders of the convertible debt instruments for converting the convertible portion into equity share capital within the said upper limit.

- (3) Where an option is to be given to the holders of the convertible debt instruments in terms of sub-regulation (2) and if one or more of such holders do not exercise the option to convert the instruments into equity share capital at a price determined in the general meeting of the shareholders, the issuer shall redeem that part of the instruments within one month from the last date by which option is to be exercised, at a price which shall not be less than its face value.
- (4) The provisions of sub-regulation (3) shall not apply if such redemption is in terms of the disclosures made in the offer document.

5. Issue of convertible debt instruments for financing (Regulation 110)

An issuer shall not issue convertible debt instruments for financing or for providing loans to or for acquiring shares of any person who is part of the promoter group or group companies:

Exception : Provided that an issuer shall be eligible to issue fully convertible debt instruments for these purposes if the period of conversion of such debt instruments is less than eighteen months from the date of issue of such debt instruments.

6. Issue of warrants (Regulation 111)

An issuer shall be eligible to issue warrants in a further public offer subject to the following conditions:

- (a) the tenure of such warrants shall not exceed eighteen months from the date of their allotment in the public issue;
- (b) a specified security may have one or more warrants attached to it;
- (c) the price or formula for determination of exercise price of the warrants shall be determined upfront and at least twenty-five per cent. of the consideration amount based on the exercise price shall also be received upfront;

Provided that in case the exercise price of warrants is based on a formula, twenty-five per cent. consideration amount based on the cap price of the price band determined for the linked equity shares or convertible securities shall be received upfront.

- (d) in case the warrant holder does not exercise the option to take equity shares against any of the warrants held by the warrant holder, within three months from the date of payment of consideration, such consideration made in respect of such warrants shall be forfeited by the issuer.

PROMOTERS' CONTRIBUTION

1. Requirement of minimum promoters' contribution not applicable in certain cases (Regulation 112)

1. The requirements of minimum promoters' contribution shall not apply in case of:
 - (a) an issuer which does **not have any identifiable promoter**;
 - (b) where the equity shares of the issuer are **frequently traded on a stock exchange for a period of at least three years** immediately preceding the reference date, and:
 - i) the issuer has **redressed at least ninety five per cent of the complaints** received from the investors till the end of the quarter immediately preceding the month of the reference date, and;
 - ii) the **issuer has been in compliance with the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 for a minimum period of three years** immediately preceding the reference date:

However, if the issuer has not complied with the provisions of the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015, relating to composition of board of directors, for any quarter during the last three years immediately preceding the date of filing of draft offer document/offer document, but is compliant with such provisions at the time of filing of draft offer document/offer document, and adequate disclosures are made in the offer document about such non-compliances during the three years immediately preceding the date of filing the draft offer document/offer document, it shall be deemed as compliance with the condition:

Provided further that where the promoters propose to subscribe to the specified securities offered to the extent greater than higher of the two options available in clause (a) of subregulation (1) of regulation 113, the subscription in excess of such percentage shall be made at a price determined in terms of the provisions of regulation 164 or the issue price, whichever is higher.

Explanation: The reference date for the purpose of computing the annualised trading turnover referred to in the said Explanation shall be the date of filing the draft offer document with the Board and in case of a fast-track issue, the date of filing the offer document with the Registrar of Companies, and before opening of the issue.

2. Minimum promoters' contribution (Regulation 113)

(1) The promoters shall contribute in the public issue as follows:

- a) either to the extent of **twenty per cent. of the proposed issue size or to the extent of twenty per cent. of the post-issue capital;**
- b) **in case of a composite issue** (i.e. further public offer cum rights issue), either to the extent of **twenty per cent. of the proposed issue size or to the extent of twenty per cent. of the post issue capital excluding the rights issue component.**

(2) **In case of a public issue or composite issue of convertible securities**, the minimum promoters' contribution shall be as follows:

- a) the promoters shall contribute **twenty per cent.** as stipulated in clause (a) or (b) of sub regulation (1), as the case may be, either by way of equity shares or by way of subscription to the convertible securities:

Provided that if the price of the equity shares allotted pursuant to conversion is not predetermined and not disclosed in the offer document, the promoters shall contribute only by way of subscription to the convertible securities being issued in the public issue and shall undertake in writing to subscribe to the equity shares pursuant to conversion of such securities.

- b) **in case of any issue of convertible securities which are convertible or exchangeable on different dates** and if the promoters' contribution is by way of equity shares (conversion price being pre-determined), such contribution shall not be at a price lower than the weighted average price of the equity share capital arising out of conversion of such securities.

(3) In case of a **further public offer or composite issue where the promoters contribute more than the stipulated minimum promoters' contribution**, the allotment with respect to excess contribution shall be made at a price determined in terms of the provisions of regulation 164 or the issue price, whichever is higher.

(4) In case **the promoters have to subscribe to equity shares or convertible securities towards promoters' contribution**, the promoters shall satisfy the requirements of this regulation at least one day prior to the date of opening of the issue and the amount of promoters' contribution shall be kept in an escrow account with a scheduled commercial bank and shall be released to the issuer along with the release of the issue proceeds:

Provided further that where the minimum promoters' contribution is more than one hundred crore rupees and the further public offer is for partly paid shares, the promoters shall bring in at least one hundred crore rupees before the date of opening of the issue and the remaining amount may be brought on a pro-rata basis before the calls are made to the public.

- (5) The SR equity shares of promoters, if any, shall be eligible towards computation of minimum promoters' contribution.

Explanation:

- (I) For the purpose of this regulation, **promoters' contribution shall be computed on the basis of the post-issue expanded capital:**
- (a) assuming full proposed conversion of convertible securities into equity shares;
 - (b) assuming exercise of all vested options, where any employee stock options are outstanding at the time of further public offer.
- (II) For computation of **"weighted average price"**:
- (a) **"weight"** means the number of equity shares arising out of conversion of such specified securities into equity shares at various stages;
 - (b) **"price"** means the price of equity shares on conversion arrived at after taking into account predetermined conversion price at various stages.

6. Securities ineligible for minimum promoters' contribution (Regulation 114)

- (1) For the computation of minimum promoters' contribution, the **following specified securities shall not be eligible:**
- (a) **specified securities acquired during the preceding three years**, if these are:
 - i) acquired for consideration other than cash and revaluation of assets or capitalisation of intangible assets is involved in such transaction; or
 - ii) resulting from a bonus issue by utilisation of revaluation reserves or unrealised profits of the issuer or from bonus issue against equity shares which are ineligible for minimum promoters' contribution;
 - (b) **specified securities pledged with any creditor** other than those for borrowings by the issuer or its subsidiaries.
- (2) **Specified securities referred to in clauses (a) of sub-regulation (1) shall be eligible for the computation of promoters' contribution**, if such securities are acquired pursuant to a scheme which has been approved by the High Court or approved by a tribunal or the Central Government under section 230 to 234 of the Companies Act, 2013.

LOCK-IN AND RESTRICTIONS ON TRANSFERABILITY

1. Lock-in of specified securities held by the promoters (Regulation 115)

The specified securities held by the promoters shall not be transferable (hereinafter referred to as "locked-in") for the periods as stipulated hereunder:

- (a) **minimum promoters' contribution** including contribution made by alternative investment funds, or foreign venture capital investors, as applicable, shall be locked-in for a period of eighteen months from the date of allotment of the further public offer:

Provided that in case the majority of the issue proceeds excluding the portion of offer for sale is proposed to be utilized for capital expenditure, then the lock-in period shall be three years from the date of allotment in the initial public offer.

- (b) **promoters' holding in excess of minimum promoters' contribution shall be locked-in for a period of six months:**

Provided that in case the majority of the issue proceeds excluding the portion of offer for sale is proposed to be utilized for capital expenditure, then the lock-in period shall be one year from the date of allotment in the initial public offer.

- (c) **The SR equity shares** shall be under lock-in until their conversion to equity shares having voting rights same as that of ordinary shares, provided they are in compliance with the other provisions of these regulations.

Explanation: For the purpose of this regulation, "capital expenditure" shall include civil work, miscellaneous fixed assets, purchase of land, building and plant and machinery, etc.

2. Lock-in of specified securities lent to stabilising agent under green shoe option (Regulation 116)

The lock-in provisions of this part **shall not apply with respect to the specified securities lent to stabilising agent for the purpose of green shoe option**, during the period starting from the date of lending of such specified securities and ending on the date on which they are returned to the lender in terms of sub-regulation (5) or (6) of regulation 153:

Provided that the specified securities shall be locked-in for the remaining period from the date on which they are returned to the lender.

3. Lock-in of party-paid securities (Regulation 117)

Where the specified securities which are subject to lock-in **are partly paid-up and the amount called-up on such specified securities is less than the amount called-up on the specified securities** issued to the public, the lock-in shall end only on the expiry of eighteen months after such specified securities have become pari passu with the specified securities issued to the public.

4. Inscription or recording of non-transferability (Regulation 118)

The **certificates of specified securities** which are subject to lock-in **shall contain the inscription "non-transferable"** and **specify the lock-in period** and in case such specified securities are dematerialised, the issuer shall ensure that the lock-in is recorded by the depository.

5. Pledge of locked-in specified securities (Regulation 119)

Specified securities (except SR equity shares) held by the promoters and locked in, **may be pledged as collateral security for a loan** granted by a scheduled commercial bank or a public financial institution or a systemically important non-banking finance company or a housing finance company, subject to the following:

- a) if the specified securities are locked-in in terms of clause (a) of regulation 115, the loan has been granted to the issuer company or its subsidiary/subsidiaries for the purpose of financing one or more of the objects of the issue and pledge of specified securities is one of the terms of sanction of the loan
- b) if the specified securities are locked-in in terms of clause (b) of regulation 115 and the pledge of specified securities is one of the terms of sanction of the loan.

6. Transferability of locked-in specified securities (Regulation 120)

Subject to the provisions of the Securities and Exchange Board of India (Substantial Acquisition of shares and Takeovers) Regulations, 2011, the specified securities except SR equity shares, held by the promoters and locked-in as per regulation 115 may be transferred to another promoter or any person of the promoter group or a new promoter or a person in control of the issuer:

Provided that lock-in on such specified securities shall continue for the remaining period with the transferee and such transferee shall not be eligible to transfer them till the lock-in period stipulated in these regulations has expired.

DISCLOSURES IN AND FILING OF OFFER DOCUMENTS

1. Disclosures in the draft offer document and the offer document

- (1) The draft offer document and the offer document shall contain **all material disclosures** which are true and adequate **to enable the applicants to take an informed investment decision**.
- (2) Without prejudice to the generality of sub-regulation (1), **the red-herring prospectus, shelf prospectus and prospectus shall contain:**
 - (i) disclosures specified in the Companies Act, 2013; and
 - (ii) disclosures specified in **Part A of Schedule VI**, subject to the provisions of **Parts C and D** thereof.
- (3) The **lead manager(s) shall exercise due diligence** and satisfy themselves about all aspects of the issue including the **veracity and adequacy of disclosures** made in the draft offer document and the offer document.
- (4) The **lead manager(s) shall call upon the issuer, its promoters and its directors** or in case of an offer for sale, the selling shareholders, to fulfil their obligations as disclosed by them in the draft offer document and the offer document and as required in terms of these Regulations.

- (5) The lead manager(s) shall ensure that the **information contained** in the offer document and the particulars as per audited financial statements in the offer document **are not more than six months old** from the issue opening date.

2. Filing of the draft offer document and offer documents (Regulation 123)

- (1) Prior to making a further public offer, the **issuer shall file three copies of the draft offer document with the Board**, in accordance with **Schedule IV**, along with fees as specified in **Schedule III**, through the lead manager(s).
- (2) The lead manager(s) shall submit the following to the Board along with the draft offer document:
- a certificate, confirming that an agreement has been entered into between the issuer and the lead manager(s)
 - a due diligence certificate as per **Form A of Schedule V**;
 - in case of an issue of convertible debt instruments, a due diligence certificate from the debenture trustee as per **Form B of Schedule V**;
 - a certificate confirming compliance of the conditions specified in **Part C of Schedule VI**.
- (3) The **issuer shall also file the draft offer document** with the stock exchange(s) where the specified securities are proposed to be listed, and shall submit to the stock exchange(s), the Permanent Account Number, bank account number and passport number of its promoters where they are individuals, and Permanent Account Number, bank account number, company registration number or equivalent and the address of the Registrar of Companies with which the promoter is registered, where the promoter is a body corporate.
- (4) The **Board may specify changes or issue observations on the draft offer document** within a period of thirty days from the later of the following dates:
- the date of receipt of the draft offer document under sub-regulation (1); or
 - the date of receipt of satisfactory reply from the lead manager(s), where the Board has sought any clarification or additional information from them; or
 - the date of receipt of clarification or information from any regulator or agency, where the Board has sought any clarification or information from such regulator or agency; or
 - the date of receipt of a copy of in principle approval letter issued by the stock exchange(s).
- (5) If the Board **specifies changes or issues observations on the draft offer document**, the issuer and the lead manager(s) shall carry out such changes in the draft offer document and shall submit to the Board an updated draft offer document complying with the observations issued by the Board and highlighting all changes made in the draft offer document before filing the offer documents with the Registrar of Companies or the appropriate authority, as applicable.

- (6) If there are any changes in the draft offer document in relation to the matters specified in **Schedule XVI**, the updated offer document or a fresh draft offer document, as the case may be, shall be filed with the Board along with fees specified in **Schedule III**.
- (7) Copy of the offer documents shall also be filed with the Board and the stock exchanges through the lead manager(s) simultaneously while filing the offer documents with Registrar of Companies.
- (8) The **draft offer document and the offer document** shall also be furnished to the Board in a soft copy in the manner as may be specified.
- (9) The lead manager(s) **shall submit the following documents to the Board after issuance of observations by the Board or after expiry of the period** stipulated in sub-regulation (4) of regulation 123 if the Board has not issued observations:
 - (a) a statement certifying that all changes, suggestions and observations made by the Board have been incorporated in the offer document;
 - (b) a due diligence certificate as per **Form C of Schedule V**, at the time of ⁸[filing] of the offer document;
 - (c) a copy of the resolution passed by the board of directors of the issuer for allotting specified securities to promoters towards amount received against promoters' contribution, before opening of the issue;
 - (d) a certificate from a Chartered Accountant, before opening of the issue, certifying that promoters' contribution has been received in accordance with these regulations, accompanying therewith the names and addresses of the promoters who have contributed to the promoters' contribution and the amount paid and credited to the bank account of the issuer by each of them towards such contribution;
 - (e) a due diligence certificate as per **Form D of Schedule V**, in the event the issuer has made a disclosure of any material development by issuing a public notice.

3. Draft offer document and offer document to be available to the public (Regulation 124)

- (1) **Filing:** The draft offer document filed with the Board shall be made public for comments, if any, for a period of **at least twenty one days from the date of filing**, by hosting it on the websites of the Board, stock exchanges where specified securities are proposed to be listed and lead manager(s) associated with the issue.
- (2) **Public announcement:** The issuer shall, within two days of filing the draft offer document with the Board, **make a public announcement** in one English national daily newspaper with wide circulation, one Hindi national daily newspaper with wide circulation and one regional language newspaper with wide circulation at the place where the registered office of the issuer is situated,

⁸ Substituted by the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) (Seventh Amendment) Regulations, 2019, w-e-f 01.01.2020 for the word "registering".

disclosing to the public the fact of filing of the draft offer document with the Board and inviting the public to provide their comments to the Board, the issuer or the lead manager(s) in respect of the disclosures made in the draft offer document.

- (3) **Filing of details of the comments:** The lead manager(s) shall, after expiry of the period stipulated in sub-regulation (1), file with the Board, details of the comments received by them or the issuer from the public, on the draft offer document, during that period and the consequential changes, if any, that are required to be made in the draft offer document.
- (4) **Documents to be hosted on website:** The issuer and the lead manager(s) shall ensure that the offer documents are hosted on the websites as required under these regulations and its contents are the same as the versions as filed with the Registrar of Companies, the Board and the stock exchanges, as applicable.
- (5) **Circulation of copies to public:** The lead manager(s) and the stock exchanges shall provide copies of the offer documents, to the public as and when requested and may charge a reasonable sum for providing a copy of the same.

PRICING

1. Face value of equity shares (Regulation 125)

The **disclosure about the face value of equity shares** shall be made in the draft offer document, offer document, advertisements and application forms, along with the price band or the issue price in identical font size.

2. Pricing (Regulation 126)

- (1) The issuer may **determine the price of equity shares**, and in case of convertible securities, the coupon rate and the conversion price, in consultation with the lead manager(s) or through the book building process, as the case may be.
- (2) The issuer **shall undertake the book building process** in the manner specified in **Schedule XIII**.

3. Price and price band (Regulation 127)

- (1) The issuer may **mention a price or a price band** in the offer document (in case of a fixed price issue) **and a floor price or a price band** in the red herring prospectus (in case of a book built issue) and determine the price at a later date before filing the prospectus with the Registrar of Companies:

Provided that the prospectus filed with the Registrar of Companies shall contain only one price or the specific coupon rate, as the case may be.

- (2) **The cap on the price band**, and the coupon rate in case of convertible debt instruments, shall be less than or equal to one hundred and twenty per cent. of the floor price.

Provided that the cap of the price band shall be at least one hundred and five percent of the floor price.

- (3) The **floor price or the final price** shall not be less than the face value of the specified securities.
- (4) Where the **issuer opts not to make the disclosure of the floor price or price band** in the red herring prospectus, the issuer shall announce the floor price or the price band at least one working day before the opening of the bid in the same newspapers in which the pre-issue advertisement was released or together with the pre-issue advertisement in the format prescribed under Part A of **Schedule X**.
- (5) The **announcement** referred to in sub-regulation (4) **shall contain relevant financial ratios** computed for both upper and lower end of the price band and also a statement drawing attention of the investors to the section title "basis of issue price" of the offer document.
- (6) The **announcement** referred to in sub-regulation (4) and the **relevant financial ratios** referred to in sub-regulation (5) **shall be disclosed on the websites** of the stock exchange(s) and shall also be pre-filled in the application forms to be made available on the websites of the stock exchange(s).

4. Differential pricing (Regulation 128)

- (1) The issuer may offer its specified securities at different prices, subject to the following:
 - a) **retail individual investors or retail individual shareholders or employees entitled for reservation** made under regulation 130 **may be offered specified securities** at a price not lower than by more than ten per cent. of the price at which net offer is made to other categories of applicants, excluding anchor investors;
 - b) in **case of a book built issue**, the price of the specified securities offered to the anchor investors shall not be lower than the price offered to other applicants;
 - c) in **case of a composite issue**, the price of the specified securities offered in the public issue may be different from the price offered in rights issue and justification for such price difference shall be given in the offer document.
 - d) in case the **issuer opts for the alternate method of book building** in terms of **Part D of Schedule XIII**, the issuer may offer the specified securities to its employees at a price not lower by more than ten per cent. of the floor price.
- (2) Discount, if any, shall be expressed in rupee terms in the offer document.

ISSUANCE CONDITIONS AND PROCEDURE

1. Allocation in the net offer (Regulation 129)

- (1) In an issue made through the book building process under sub-regulation (1) of regulation 103, the allocation in the net offer category shall be as follows:

- a) not less than thirty five per cent. to retail individual investors;
- b) not less than fifteen per cent. to non-institutional investors;
- c) not more than fifty per cent. to qualified institutional buyers, five per cent. of which shall be allocated to mutual funds:

Provided that the unsubscribed portion in either of the categories specified in clauses (a) or (b) may be allocated to applicants in any other category:

Provided further that in addition to five per cent. allocation available in terms of clause (c), mutual funds shall be eligible for allocation under the balance available for qualified institutional buyers.

- (2) In an issue made through the book building process under sub-regulation (2) of regulation 103, the allocation in the net offer category shall be as follows:

- (a) not more than ten per cent. to retail individual investors;
- (b) not more than fifteen per cent. to non-institutional investors;
- (c) not less than seventy five per cent. to qualified institutional buyers, five per cent. of which shall be allocated to mutual funds:

Provided that the unsubscribed portion in either of the categories specified in clauses (a) or (b) may be allocated to applicants in the other category:

Provided further that in addition to five per cent. allocation available in terms of clause (c), mutual funds shall be eligible for allocation under the balance available for qualified institutional buyers.

- (3) In an issue made through the book building process, the issuer may allocate up to sixty per cent. of the portion available for allocation to qualified institutional buyers to anchor investors in accordance with the conditions specified in this regard in **Schedule XIII**.

- (3A) In **an issue made through book building process**, the allocation in the non-institutional investors' category shall be as follows:

- (a) **one third** of the portion available to non-institutional investors shall be reserved for applicants **with application size of more than two lakh rupees and up to ten lakh rupees**;
- (b) **two third** of the portion available to non-institutional investors shall be reserved for applicants **with application size of more than ten lakh rupees** :

Provided that the unsubscribed portion in either of the sub-categories specified in clauses (a) or (b) may be allocated to applicants in the other sub-category of non-institutional investors.

- (4) In **an issue made other than through the book building process**, allocation in the net offer category shall be made as follows:

- (a) **minimum fifty per cent. to retail individual investors**; and
- (b) **remaining to:**
 - (i) **individual applicants** other than retail individual investors; and
 - (ii) **other investors** including corporate bodies or institutions, irrespective of the number of specified securities applied for;

Provided that the unsubscribed portion in either of the categories specified in clauses (a) or (b) may be allocated to applicants in the other category.

Explanation: For the purpose of sub-regulation (4), if the retail individual investor category is entitled to more than fifty per cent. of the issue size on a proportionate basis, the retail individual investors shall be allocated that higher percentage.

2. **Reservation on a competitive basis (Regulation 130)**

- (1) The issuer may make reservations on a competitive basis out of the issue size excluding promoters' contribution in favour of the following categories of persons:
 - (a) employees;
 - (b) shareholders (other than promoters and promoter group) of listed subsidiaries or listed promoter companies:

However, it is provided that the issuer shall not make any reservation for the lead manager(s), registrar, syndicate member(s), their promoters, directors and employees and for the group or associate companies (as defined under the Companies Act, 2013) of the lead manager(s), registrar and syndicate member(s) and their promoters, directors and employees.

- (2) **In a further public offer**, other than in a composite issue, the issuer may make a reservation on a competitive basis out of the issue size excluding promoters' contribution **for the existing retail individual shareholders of the issuer**.
- (3) **Required Conditions:** The reservations on competitive basis shall be subject to following conditions:
 - (a) **Limit on reservation for employees:** the aggregate of reservation for employees shall not exceed five per cent. of the post-issue capital of the issuer and the value of allotment to any employee shall not exceed two lakhs rupees:

Provided that in the event of under-subscription in the employee reservation portion, the unsubscribed portion may be allotted on a proportionate basis, for a value in excess of two lakhs rupees, subject to the total allotment to an employee not exceeding five lakhs rupees.
 - (b) **Limit on reservation for shareholders:** reservation for shareholders shall not exceed ten per cent. of the issue size;

- (c) **When no further application can be made:** no further application for subscription in the net offer can be made by persons (except an employee and retail individual shareholder of the listed issuer and retail individual shareholders of listed subsidiaries of listed promoter companies) in favour of whom reservation on a competitive basis is made;
 - (d) **Addition of unreserved portion to other reserved category :** any unsubscribed portion in any reserved category may be added to any other reserved category/categories and the unsubscribed portion, if any, after such inter-se adjustments amongst the reserved categories shall be added to the net offer category;
 - (e) **Undersubscription to spill over in net public offer:** in case of under-subscription in the net offer category, spill-over to the extent of undersubscription shall be permitted from the reserved category to the net public offer.
- (4) An applicant in any reserved category may make an application for any number of specified securities, but not exceeding the reserved portion for that category.

Abridged prospectus (Regulation 131)

- (1) The abridged prospectus shall **contain the disclosures** as specified in **Part E of Schedule VI** and shall not contain any matter extraneous to the contents of the offer document.
- (2) **Every application** form distributed by the issuer or any other person in relation to an issue **shall be accompanied by a copy of the abridged prospectus**.

Availability of issue material (Regulation 133)

The lead manager(s) shall ensure availability of the offer document and other issue material including application forms to stock exchanges, syndicate members, registrar to issue, registrar and share transfer agents, depository participants, stock brokers, underwriters, bankers to the issue, investors' associations and self-certified syndicate banks before the opening of the issue.

Prohibition on payment of incentives (Regulation 134)

Any person connected with the issue, shall not offer any incentive, whether direct or indirect, in any manner, whether in cash or kind or services or otherwise to any person for making an application in the initial public offer, except for fees or commission for services rendered in relation to the issue.

Security deposit (Regulation 135)

- (1) **Deposit of security amount:** The issuer shall, before the opening of the subscription list, deposit with the designated stock exchange, an amount calculated at the rate of one per cent. of the issue size available for subscription to the public in the manner specified by the Board and/or the stock exchange(s).
- (2) The amount specified above shall be **refundable or forfeitable** in the manner specified by the Board.

Underwriting (Regulation 136)

- (1) **Appointment of underwriters:** If the issuer making a further public offer, other than through the book building process, desires to have the issue underwritten, it shall appoint merchant bankers or stock brokers, registered with the Board, to act as underwriters.
- (2) If the **issuer makes a public issue through the book building process**,
 - (a) the issue shall be underwritten by lead manager(s) and syndicate member(s):
 Provided that at least seventy five per cent. of the net offer proposed to be compulsorily allotted to qualified institutional buyers for the purpose of compliance of the eligibility conditions specified in sub-regulation (2) of regulation 103, shall not be underwritten.
 - (b) the issuer shall, prior to filing the prospectus, enter into underwriting agreement with the lead manager(s), and syndicate member(s), indicating therein the number of specified securities which they shall subscribe to at the predetermined price in the event of undersubscription in the issue.
 - (c) if the syndicate member(s) fail to fulfil their underwriting obligations, the lead manager(s) shall fulfil the underwriting obligations.
 - (d) the lead manager(s) and syndicate member(s) shall not subscribe to the issue in any manner except for fulfilling their underwriting obligations.
 - (e) in case of every underwritten issue, the lead manager(s) shall undertake minimum underwriting obligations as specified in the Securities and Exchange Board of India (Merchant Bankers) Regulations, 1992.
 - (f) where the issue is required to be underwritten, the underwriting obligations should at least be to the extent of minimum subscription.

Monitoring agency (Regulation 137)

- (1) If the issue size, excluding the size of offer for sale by selling shareholders, exceeds one hundred crore rupees, the issuer shall make arrangements for the use of proceeds of the issue to be monitored by a credit rating agency registered with the Board:
 Provided that nothing contained in this clause shall apply to an issue of specified securities made by a bank or public financial institution or an insurance company.
- (2) The monitoring agency shall submit its report to the issuer in the format specified in **Schedule XI** on a quarterly basis, till hundred per cent of the proceeds of the issue have been utilised.
- (3) The board of directors and the management of the issuer shall provide their comments on the findings of the monitoring agency as specified in **Schedule XI**.

- (4) The issuer shall, within forty five days from the end of each quarter, publicly disseminate the report of the monitoring agency by uploading the same on its website as well as submitting the same to the stock exchange(s) on which its equity shares are listed.

Issue-related advertisements (Regulation 139)

- (1) Subject to the provisions of the Companies Act, 2013, the issuer shall, after filing the red herring prospectus (in case of a book built issue) or prospectus (in case of fixed price issue) with the Registrar of Companies, make a pre-issue advertisement in one English national daily newspaper with wide circulation, Hindi national daily newspaper with wide circulation and one regional language newspaper with wide circulation at the place where the registered office of the issuer is situated.
- (2) The pre-issue advertisement shall be in the format and shall contain the disclosures specified in **Part A of Schedule X**.
Provided that the disclosures in relation to price band or floor price and financial ratios contained therein shall be applicable only where the issuer opts to announce the price band or floor price along with the pre-issue advertisement pursuant to sub-regulation (4) of regulation 127.
- (3) The issuer may release advertisements for issue opening and issue closing, which shall be in the formats specified in **Parts B and C of Schedule X**.
- (4) During the period the issue is open for subscription, no advertisement shall be released giving an impression that the issue has been fully subscribed or oversubscribed or indicating investors' response to the issue.

Opening of the issue (Regulation 140)

- (1) Subject to the compliance with the provisions of the Companies Act, 2013, a public issue may be opened within twelve months from the date of issuance of the observations by the Board under sub-regulation (4) of regulation 123; or
Provided that in case of a fast track issue, the issue shall open within the period specifically stipulated under the Companies Act, 2013.
- (2) In case of **shelf prospectus**, the first issue may be opened within three months of issuance of observations by the Board.
- (3) **The issue shall be opened** after at least three working days from the date of filing the red herring prospectus with the Registrar of Companies in case of book built issues and prospectus with the Registrar of Companies in case of fixed price issues.

Minimum subscription (Regulation 141)

- (1) The minimum subscription to be received in the issue shall be **at least ninety per cent. of the offer** through the offer document, except in case of an offer for sale of specified securities.

- (2) In the **event of non-receipt of minimum subscription** referred to in sub-regulation (1), all application monies received shall be refunded to the applicants forthwith, but not later than four days from the closure of the issue.

Period of subscription (Regulation 142)

- (1) A further public issue shall be kept open for **at least three working days** and not more than ten working days.
- (2) **In case of a revision in the price band**- the issuer shall extend the bidding (issue) period disclosed in the red herring prospectus, for a **minimum period of three working days**, subject to the provisions of sub-regulation (1).
- (3) In case of force majeure, banking strike or similar circumstances, the issuer may, for reasons to be recorded in writing, **extend the bidding (issue) period** disclosed in the red herring prospectus (in case of a book built issue) or the issue period disclosed in the prospectus (in case of a fixed price issue), **for a minimum period of three working days**, subject to the provisions of sub-regulation (1).

Application and minimum application value (Regulation 143)

- (1) A person shall not make an application in the net offer category for a number of specified securities that exceeds the total number of specified securities offered to public.

Provided that the maximum application by non-institutional investors shall not exceed total number of specified securities offered in the issue less total number of specified securities offered in the issue to qualified institutional buyers.

- (2) The issuer shall stipulate in the offer document the minimum application size in terms of number of specified securities which shall fall within the range of minimum application value of ten thousand rupees to fifteen thousand rupees.
- (3) The issuer shall invite applications in multiples of the minimum application value, an illustration whereof is given in **Part B of Schedule XIV**.
- (4) The minimum sum payable on application per specified security shall be at least twenty five per cent. of the issue price:

Provided that in case of an offer for sale, the full issue price for each specified security shall be payable at the time of application.

Explanation: For the purpose of this regulation, "minimum application value" shall be with reference to the issue price of the specified securities and not with reference to the amount payable on application.

Manner of calls (Regulation 144)

If the issuer proposes to receive subscription monies in calls, it shall ensure that the **outstanding subscription money is called within twelve months from the date of allotment in the issue**.

If any **applicant fails** to pay the call money within the said twelve months, the equity shares on which there are calls in arrear along with the subscription money already paid on such shares shall be **forfeited**:

Exception when it shall not be necessary to call the outstanding subscription money within twelve months, **if the issuer has appointed a monitoring agency** in terms of regulation 137.

Allotment procedure and basis of allotment (Regulation 145)

- (1) **Allotment of public issue:** The issuer shall not make an allotment pursuant to a public issue if the number of prospective allottees is less than one thousand.
- (2) **When no allotment shall be made:** The issuer shall not make any allotment in excess of the specified securities offered through the offer document except in case of oversubscription for the purpose of rounding off to make allotment, in consultation with the designated stock exchange.

Provided that in case of oversubscription, an allotment of not more than one per cent. of the net offer to public may be made for the purpose of making allotment in minimum lots.

- (3) **Allotment of securities:** The allotment of specified securities to applicants other than retail individual investors non-institutional investors and anchor investors **shall be on proportionate basis within the specified investor categories** and the number of securities allotted shall be rounded off to the nearest integer, subject to minimum allotment being equal to the minimum application size as determined and disclosed by the issuer:

Provided that value of specified securities allotted to any person, except in case of employees, in pursuance of reservation made under clause (a) of sub-regulation (1) or clause (a) of sub regulation (2) of regulation 130, shall not exceed two lakhs rupees.

- (4) **The allotment of specified securities to each retail individual investor** shall not be less than the minimum bid lot, subject to availability of shares in retail individual investor category, and the remaining available shares, if any, shall be allotted on a proportionate basis.
- (4A) **The allotment of specified securities to each non-institutional investor** shall not be less than the minimum application size, subject to the availability of shares in non-institutional investors' category, and the remaining shares, if any, shall be allotted on a proportionate basis in accordance with the conditions specified in this regard in Schedule XIII of these regulations.
- (5) **Finalised basis of allotment :** The authorised employees of the designated stock exchange along with the lead manager(s) and registrars to the issue shall ensure that the basis of allotment is finalised in a fair and proper manner in accordance with the allotment procedure as specified in **Part A of Schedule XIV**.

Allotment, refund and payment of interest (Regulation 146)

- (1) The issuer and lead manager(s) shall ensure that specified securities are allotted and/or application monies are refunded or unblocked within such period as may be specified by the Board.

- (2) The lead manager(s) shall ensure that the allotment, credit of dematerialised securities, refunding or unblocking of application monies, as may be applicable, are done electronically.
- (3) Where specified securities are not allotted and/or application monies are not refunded or unblocked within the period stipulated in sub-regulation (1) above, the issuer shall undertake to pay interest at the rate of fifteen per cent. per annum to the investors and within such time as disclosed in the offer document and the lead manager(s) shall ensure the same.

Post-issue Advertisements (Regulation 147)

- (1) **Issue of advertisements with details:** The lead manager(s) shall ensure that advertisement giving details relating to subscription, basis of allotment, number, value and percentage of all applications including ASBA, number, value and percentage of successful allottees for all applications including ASBA, date of completion of despatch of refund orders, as applicable, or instructions to self-certified syndicate banks by the registrar, date of credit of specified securities and date of filing of listing application, etc. is released within ten days from the date of completion of the various activities in at least one English national daily newspaper with wide circulation, one Hindi national daily newspaper with wide circulation and one regional language daily newspaper with wide circulation at the place where registered office of the issuer is situated.
- (2) **Placing on website of stock exchange:** Details specified in sub regulation (1) shall also be placed on the websites of the stock exchanges.

Post-issue responsibilities of the lead manager(s) (Regulation 148)

- The lead manager(s) shall regularly monitor redressal of investor grievances arising from any issue related activities. He shall continue to be responsible for post-issue activities till the applicants have received the securities certificates, credit to their demat account or refund of application monies and the listing agreement is entered into by the issuer with the stock exchange and listing or trading permission is obtained.
- The lead manager(s) shall be responsible and co-ordinate with the registrars to the issue and with various intermediaries at regular intervals after the closure of the issue to monitor the flow of applications from syndicate member(s) or collecting bank branches and or self-certified syndicate banks, processing of the applications including application form for ASBA and other matters till the basis of allotment is finalised, credit of the specified securities to the demat accounts of the allottees and unblocking of ASBA accounts/ despatch of refund orders are completed and securities are listed, as applicable.
- Any act of omission or commission on the part of any of the intermediaries noticed by the lead manager(s) shall be duly reported by them to the Board.
- In case there is a devolvement on underwriters, the lead manager(s) shall ensure that the notice for devolvement containing the obligation of the underwriters is issued within a period of ten days from the date of closure of the issue.

- In case of undersubscribed issues that are underwritten, the lead manager(s) shall furnish information to the Board in respect of underwriters who have failed to meet their underwriting devolvement in the format specified in **Schedule XVIII**.

Release of subscription money (Regulation 149)

- (1) The lead manager(s) shall confirm to the bankers to the issue by way of copies of listing and trading approvals that all **formalities in connection with the issue have been completed** and that the **banker is free to release the money to the issuer or release the money for refund** in case of failure of the issue.
- (2) In case the **issuer fails to obtain listing or trading permission** from the stock exchanges where the specified securities were listed, **it shall refund**, through verifiable means, the entire monies received within four days of receipt of intimation from stock exchanges rejecting the application for listing of specified securities and if monies are not repaid within the specified period, the issuer and every director of the company who is an officer in default shall, on and from the expiry of the fourth day, be jointly and severally liable to repay that money with interest at the rate of fifteen per cent. per annum.
- (3) The lead manager(s) shall ensure that the **monies received in respect of the issue are released to the issuer** in compliance with the provisions of the Section 40 (3) of the Companies Act, 2013, as applicable.

Post- issue reports (Regulation 150)

The lead manager(s) shall submit a final post-issue report as specified in **Part A of Schedule XVII**, along with a due diligence certificate as per the format specified in **Form F of Schedule V**, within seven days of the date of finalization of basis of allotment or within seven days of refund of money in case of failure of issue.

MISCELLANEOUS

Restriction on further capital issues (Regulation 151)

An issuer shall not make any further issue of specified securities in any manner whether by way of public issue, rights issue, preferential issue, qualified institutions placement, issue of bonus shares or otherwise, except pursuant to an employee stock option scheme:

- in case of a fast track issue**, during the period between the date of filing the offer document (in case of a book built issue) or prospectus (in case of a fixed price issue) with the Registrar of Companies and the listing of the specified securities offered through the offer document or refund of application monies; or
- in case of other issues**, during the period between the date of filing the draft offer document and the listing of the specified securities offered through the offer document or refund of application monies; unless full disclosures regarding the total number of specified securities or amount

proposed to be raised from such further issue are made in such draft offer document or offer document, as the case may be.

Price stabilisation through green shoe option (Regulation 153)

- (1) An issuer may provide green shoe option for stabilising the post listing price of its specified securities, **subject to the following**:
 - a) the issuer has been authorized, by a resolution passed in the general meeting of shareholders approving the public issue, to allot specified securities to the stabilising agent, if required, on the expiry of the stabilisation period;
 - b) the issuer has appointed a lead manager as a stabilising agent, who shall be responsible for the price stabilisation process;
 - c) prior to filing the draft offer document, the issuer and the stabilising agent have entered into an agreement, stating all the terms and conditions relating to the green shoe option including fees charged and expenses to be incurred by the stabilising agent for discharging its responsibilities;
 - d) prior to filing the offer document, the stabilising agent has entered into an agreement with the promoters or pre-issue shareholders or both for borrowing specified securities from them in accordance with clause (g) of this sub-regulation, specifying therein the maximum number of specified securities that may be borrowed for the purpose of allotment or allocation of specified securities in excess of the issue size (hereinafter referred to as the "over- allotment"), which shall not be in excess of fifteen per cent. of the issue size;
 - e) subject to clause (d), the lead manager, in consultation with the stabilising agent, shall determine the amount of specified securities to be over-allotted in the public issue;
 - f) the draft offer document and offer document shall contain all material disclosures about the green shoe option specified in this regard in **Part A of Schedule VI**;
 - g) in case of an initial public offer pre-issue shareholders and promoters and in case of a further public offer pre-issue shareholders holding more than five per cent. specified securities and promoters, may lend specified securities to the extent of the proposed over-allotment;
 - h) the specified securities borrowed shall be in dematerialised form and allocation of these securities shall be made pro-rata to all successful applicants.
- (2) For the purpose of stabilisation of post-listing price of the specified securities, the **stabilising agent shall determine the relevant aspects** including the timing of buying such securities, quantity to be bought and the price at which such securities are to be bought from the market.
- (3) The **stabilisation process shall be available for a period not exceeding thirty days** from the date on which trading permission is given by the stock exchanges in respect of the specified securities allotted in the public issue.

- (4) The stabilising agent shall **open a special account**, distinct from the issue account, with a bank for crediting the monies received from the applicants against the over-allotment and a special account with a depository participant for crediting specified securities to be bought from the market during the stabilisation period out of the monies credited in the special bank account.
- (5) The specified securities bought from the market and credited in the special account with the depository participant **shall be returned to the promoters or pre-issue shareholders immediately**, in any case not later than two working days after the end of the stabilization period.
- (6) **On expiry of the stabilisation period**, if the stabilising agent has not been able to buy specified securities from the market to the extent of such securities over-allotted, the issuer shall allot specified securities at issue price in dematerialised form to the extent of the shortfall to the special account with the depository participant, within five days of the closure of the stabilisation period and such specified securities shall be returned to the promoters or pre-issue shareholders by the stabilising agent in lieu of the specified securities borrowed from them and the account with the depository participant shall be closed thereafter.
- (7) The **issuer shall make a listing application** in respect of the further specified securities allotted under sub-regulation (6), **to all the stock exchanges** where the specified securities allotted in the public issue are listed and the provisions of Chapter VII shall not be applicable to such allotment.
- (8) The stabilising agent shall **remit the monies with respect to the specified securities allotted** under sub-regulation (6) to the issuer from the special bank account.
- (9) Any **monies left** in the special bank account after remittance of monies to the issuer under subregulation (8) and deduction of expenses incurred by the stabilising agent for the stabilisation process **shall be transferred to the Investor Protection and Education Fund** established by the Board and the special bank account shall be closed soon thereafter.
- (10) The stabilising agent shall **submit a report to the stock exchange** on a daily basis during the stabilisation period and a final report to the Board in the format specified in **Schedule XV**.
- (11) The stabilising agent shall **maintain a register for a period of at least three years** from the date of the end of the stabilisation period and such register shall contain the following particulars:
 - a) The names of the promoters or pre-issue shareholders from whom the specified securities were borrowed and the number of specified securities borrowed from each of them;
 - b) The price, date and time in respect of each transaction effected in the course of the stabilisation process; and
 - c) The details of allotment made by the issuer on expiry of the stabilisation process.

THE SECURITIES AND EXCHANGE BOARD OF INDIA (SUBSTANTIAL ACQUISITION OF SHARES AND TAKEOVERS) REGULATIONS, 2011

INTRODUCTION

Due to the growth of Mergers & Acquisitions activity in India as the preferred mode of restructuring, the increasing intricacy of takeover market, the decade long regulatory experience and various judicial pronouncements, it felt necessary to periodically review the Takeover Regulations, 1997.

Accordingly, SEBI established a Takeover Regulations Advisory Committee (TRAC) in September 2009 under the Chairmanship of (Late) Shri. C. Achuthan, Former Presiding Officer, Securities Appellate Tribunal (SAT) for this purpose. After public consultation on the report submitted by TRAC, SEBI came out with the SAST Regulations, 2011 which were notified on September 23, 2011. Thereby, Takeover Regulations, 1997 stand repealed from October 22, 2011, i.e. the date on which SAST Regulations, 2011 come into force.

Vide the notification F. No. LAD-NRO/GN/2011-12/24/30181 dated September 23, 2011, the SAST Regulations, 2011 were notified with effect from October 22, 2011.

Meaning of Takeovers & Substantial acquisition of shares: When an “**acquirer**” takes over the control of the “**Target Company**”, it is termed as Takeover. When an acquirer acquires “**substantial quantity of shares or voting rights**” of the Target Company, it results into substantial acquisition of shares.

Applicability: These regulations shall apply to direct and indirect acquisition of shares or voting rights in, or control over Target Company:

Provided that these regulations shall not apply to direct and indirect acquisition of shares or voting rights in, or control over a company listed without making a public issue, on the Innovators Growth Platform of a recognised stock exchange.

RELEVANT TERMINOLOGIES [Regulation 2(1)]

“**acquirer**” means any person who, directly or indirectly, **acquires or agrees to acquire** whether by himself, or through, or with persons acting in concert with him, **shares or voting rights in, or control over a target company**;

“**acquisition**” means, directly or indirectly, **acquiring or agreeing to acquire shares or voting rights in, or control over**, a target company;

“**control**” includes the **right to appoint majority of the directors or to control the management or policy decisions** exercisable by a person or persons acting individually or in concert, directly or indirectly, including by virtue of their shareholding or management rights or shareholders agreements or voting agreements or in any other manner:

Provided that a director or officer of a target company shall not be considered to be in control over such target company, merely by virtue of holding such position;

“disinvestment” means the direct or indirect **sale by the Central Government or any State Government or by a government company**, as the case may be, **of shares or voting rights in, or control over, a target company**, which is a public sector undertaking;

“offer period” means the **period between the date of entering into an agreement**, formal or informal, **to acquire shares, voting rights in, or control over a target company** requiring a public announcement, or the date of the public announcement, as the case may be, and the date on which the payment of consideration to shareholders who have accepted the open offer is made, or the date on which open offer is withdrawn, as the case may be;

“persons acting in concert” (PAC) means,—

- (1) **persons who**, with a common objective or purpose of acquisition of shares or voting rights in, or exercising control over a target company, pursuant to an agreement or understanding, formal or informal, directly or indirectly **co-operate for acquisition of shares or voting rights in, or exercise of control over the target company**.
- (2) Without prejudice to the generality of the foregoing, the **persons falling within the following categories** shall be deemed to be persons acting in concert with other persons within the same category—
 - (i) a company, its holding company, subsidiary company and any company under the same management or control;
 - (ii) a company, its directors, and any person entrusted with the management of the company;
 - (iii) directors of companies referred to in item (i) and (ii) of this sub-clause and associates of such directors;
 - (iv) promoters and members of the promoter group;
 - (v) immediate relatives;
 - (vi) a mutual fund, its sponsor, trustees, trustee company, and asset management company;
 - (vii) a collective investment scheme and its collective investment management company, trustees and trustee company;
 - (viii) a venture capital fund and its sponsor, trustees, trustee company and asset management company;
 - (viiia) an alternative investment fund and its sponsor, trustees, trustee company and manager;
 - (ix) Omitted

- (x) a merchant banker and its client, who is an acquirer;
- (xi) a portfolio manager and its client, who is an acquirer;
- (xii) banks, financial advisors and stock brokers of the acquirer, or of any company which is a holding company or subsidiary of the acquirer, and where the acquirer is an individual, of the immediate relative of such individual:

Provided that this sub-clause shall not apply to a bank whose sole role is that of providing normal commercial banking services or activities in relation to an open offer under these regulations;

- (xiii) an investment company or fund and any person who has an interest in such investment company or fund as a shareholder or unitholder having not less than 10 per cent of the paid-up capital of the investment company or unit capital of the fund, and any other investment company or fund in which such person or his associate holds not less than 10 per cent of the paid-up capital of that investment company or unit capital of that fund:

Provided that nothing contained in this sub-clause shall apply to holding of units of mutual funds registered with the Board;

Explanation.— For the purposes of this clause “associate” of a person means,—

- (a) any immediate relative of such person;
- (b) trusts of which such person or his immediate relative is a trustee;
- (c) partnership firm in which such person or his immediate relative is a partner; and
- (d) members of Hindu undivided families of which such person is a coparcener;

“public sector undertaking” means a target company in which, directly or indirectly, majority of shares or voting rights or control is held by the Central Government or any State Government or Governments, or partly by the Central Government and partly by one or more State Governments;

“shares” means shares in the equity share capital of a target company carrying voting rights, and includes any security which entitles the holder thereof to exercise voting rights.

Explanation— For the purpose of this clause shares will include all depository receipts carrying an entitlement to exercise voting rights in the target company.

“target company” means a **company** and includes a body corporate or corporation established under a Central legislation, State legislation or Provincial legislation for the time being in force, **whose shares are listed on a stock exchange.**

SUBSTANTIAL ACQUISITION OF SHARES, VOTING RIGHTS OR CONTROL

Substantial acquisition of shares or voting rights (Section 3)

Threshold limits for acquisition of shares/voting rights:

- (1) No acquirer shall acquire shares or voting rights in a target company which taken together with shares or voting rights, if any, held by him and by persons acting in concert with him in such target company, entitle them to exercise twenty-five per cent or more of the voting rights in such target company unless the acquirer makes a public announcement of an open offer for acquiring shares of such target company in accordance with these regulations.

Thus, accordingly, an acquirer, who (along with PACs, if any) **holds less than 25% shares or voting rights in a target company** and agrees to acquire shares or acquires shares which along with his/ PAC's existing shareholding **would entitle him to exercise 25% or more shares or voting rights** in a target company, will need to make an open offer before acquiring such additional shares.

- (2) No acquirer, who together with persons acting in concert with him, has acquired and holds in accordance with these regulations shares or voting rights in a target company entitling them to exercise twenty-five per cent or more of the voting rights in the target company but less than the maximum permissible non-public shareholding, shall acquire within any financial year additional shares or voting rights in such target company entitling them to exercise more than five per cent of the voting rights, unless the acquirer makes a public announcement of an open offer for acquiring shares of such target company in accordance with these regulations:

Provided that the acquisition **beyond five per cent but upto ten per cent of the voting rights** in the target company shall be permitted for the financial year 2020-21 only in respect of acquisition by a promoter pursuant to preferential issue of equity shares by the target company.

Provided that such acquirer shall not be entitled to acquire or enter into any agreement to acquire shares or voting rights exceeding such number of shares as would take the aggregate shareholding pursuant to the acquisition above the maximum permissible non-public shareholding.

Provided further that, acquisition pursuant to a resolution plan approved under section 31 of the Insolvency and Bankruptcy Code, 2016 shall be exempt from the obligation under the proviso to the sub-regulation (2) of regulation 3.]

Explanation— For purposes of determining the quantum of acquisition of additional voting rights under this sub-regulation,—

- (i) gross acquisitions alone shall be taken into account regardless of any intermittent fall in shareholding or voting rights whether owing to disposal of shares held or dilution of voting rights owing to fresh issue of shares by the target company.

- (ii) in the case of acquisition of shares by way of issue of new shares by the target company or where the target company has made an issue of new shares in any given financial year, the difference between the pre-allotment and the post-allotment percentage voting rights shall be regarded as the quantum of additional acquisition .

According to this clause, an acquirer who (along with PACs, if any) **holds 25% or more but less than the maximum permissible non-public shareholding in a target company**, can acquire additional shares in the target company as would entitle him to exercise more than 5% of the voting rights in any financial year ending March 31, only after making an open offer.

- (3) For the purposes of sub-regulation (1) and sub-regulation (2), acquisition of shares by any person, such that the **individual shareholding of such person acquiring shares exceeds the stipulated thresholds**, shall also be attracting the obligation to make an open offer for acquiring shares of the target company irrespective of whether there is a change in the aggregate shareholding with persons acting in concert.
- (4) Nothing contained in this regulation shall apply to acquisition of shares or voting rights of a company by the promoters or shareholders in control, in terms of the provisions of Chapter VI-A of Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009.
- (5) For the purpose of this regulation, any reference to “**twenty-five per cent**” in case of listed entity which has **listed its specified securities on Innovators Growth Platform** shall be read as “**forty-nine per cent**”.

Acquisition of control (Regulation 4)

Irrespective of acquisition or holding of shares or voting rights in a target company, no acquirer shall acquire, directly or indirectly, control over such target company unless the **acquirer makes a public announcement of an open offer** for acquiring shares of such target company in accordance with these regulations.

An **Open Offer** is an offer made by the acquirer to the shareholders of the target company inviting them to tender their shares in the target company at a particular price. The primary purpose of an open offer is to provide an exit option to the shareholders of the target company on account of the change in control or substantial acquisition of shares, occurring in the target company.

If an acquirer has agreed to acquire or acquired control over a target company or shares or voting rights in a target company which would be in excess of the threshold limits, then the acquirer is required to make an open offer to shareholders of the target company.

A **Voluntary Open** offer under Regulation 6, is an offer made by a person who himself or through Persons acting in concert ,if any, **holds 25% or more shares or voting rights in the target company but less than the maximum permissible non-public shareholding limit**.

Offer Price is the price at which the acquirer announces to acquire shares from the public shareholders under the open offer. The offer price shall not be less than the price as calculated under regulation 8 of the SAST Regulations, 2011 for frequently or infrequently traded shares. Acquirer can make an upward revision to the offer price at any time up to 3 working days prior to the opening of the offer.

OBLIGATIONS:

Following are the obligations of the Directors, Acquirers and of the Target company:

(i) Directors of the target company (Regulation 24)

- (1) **Person representing the acquirer or PAC shall be appointed as Director:** During the offer period, no person representing the acquirer or any person acting in concert with him shall be appointed as director on the board of directors of the target company, whether as an additional director or in a casual vacancy.

Provided that after an initial period of fifteen working days from the date of detailed public statement, appointment of persons representing the acquirer or persons acting in concert with him on the board of directors may be effected in the event the acquirer deposits in cash in the escrow account referred to in regulation 17, the entire consideration payable under the open offer.

Provided further that where the acquirer has specified conditions to which the open offer is subject in terms of clause (c) of sub-regulation (1) of regulation 23, no director representing the acquirer may be appointed to the board of directors of the target company during the offer period unless the acquirer has waived or attained such conditions and complies with the requirement of depositing cash in the escrow account.

- (2) **In case of ⁹conditional open offer, the acquirer and PAC shall not be entitled to appoint any director representing them on the BoD:** Where an open offer is made conditional upon minimum level of acceptances, the acquirer and persons acting in concert shall, notwithstanding anything contained in these regulations, and regardless of the size of the cash deposited in the escrow account referred to regulation 17, not be entitled to appoint any director representing the acquirer or any person acting in concert with him on the board of directors of the target company during the offer period.

'Minimum level of acceptance' implies minimum number of shares which the acquirer desires under the said conditional offer. If the number of shares validly tendered in the conditional offer, are less than the minimum level of acceptance stipulated by the acquirer, then the acquirer is not bound to accept any shares under the offer.

- (3) **No new director to be introduced during pendency of competing offers:** During the pendency of ¹⁰competing offers, notwithstanding anything contained in these regulations, and regardless of

⁹ An offer in which the acquirer has stipulated a minimum level of acceptance is known as a 'conditional offer'.

¹⁰ Competitive offer is an offer made by a person, other than the acquirer who has made the first public announcement.

the size of the cash deposited in the escrow account referred to in regulation 17, by any acquirer or person acting in concert with him, there shall be no induction of any new director to the board of directors of the target company:

In case of vacancy: that in the event of death or incapacitation of any director, the vacancy arising therefrom may be filled by any person subject to approval of such appointment by shareholders of the target company by way of a postal ballot.

- (4) **No participation in any deliberations of the BoD:** In the event the acquirer or any person acting in concert is already represented by a director on the board of the target company, such director shall not participate in any deliberations of the board of directors of the target company or vote on any matter in relation to the open offer.

(ii) **Obligations of the acquirer (Regulation 25)**

- (1) **Financial arrangements for fulfilling the payment obligations:** Prior to making the public announcement of an open offer for acquiring shares under these regulations, the acquirer shall ensure that firm financial arrangements have been made for fulfilling the payment obligations under the open offer and that the acquirer is able to implement the open offer, subject to any statutory approvals for the open offer that may be necessary.

- (2) **In case of failure to declare alienation of assets:** In the event the acquirer has not declared an intention in the detailed public statement and the letter of offer to alienate any material assets of the target company or of any of its subsidiaries whether by way of sale, lease, encumbrance or otherwise outside the ordinary course of business, the acquirer, where he has acquired control over the target company, shall be debarred from causing such alienation for a period of two years after the offer period:

Provided that in the event the target company or any of its subsidiaries is required to so alienate assets despite the intention to alienate not having been expressed by the acquirer, such alienation shall require a special resolution passed by shareholders of the target company, by way of a postal ballot and the notice for such postal ballot shall *inter alia* contain reasons as to why such alienation is necessary.

- (3) **Assurance of true and fair particulars of requisite sources:** The acquirer shall ensure that the contents of the public announcement, the detailed public statement, the letter of offer and the post-offer advertisement are true, fair and adequate in all material aspects and not misleading in any material particular, and are based on reliable sources, and state the source wherever necessary.
- (4) **Not entitled to sell shares during offer period:** The acquirer and persons acting in concert with him shall not sell shares of the target company held by them, during the offer period.
- (5) **Jointly and severally responsible for their obligations:** The acquirer and persons acting in concert with him shall be jointly and severally responsible for fulfillment of applicable obligations under these regulations.

(iii) **Obligations of the target company(Regulation 26)**

- (1) **Conduct of business consistent with past practice:** Upon a public announcement of an open offer for acquiring shares of a target company being made, the board of directors of such target company shall ensure that during the offer period, the business of the target company is conducted in the ordinary course consistent with past practice.
- (2) During the offer period, unless the approval of shareholders of the target company by way of a special resolution by postal ballot is obtained, the board of directors of either the target company or any of its subsidiaries shall not,—
 - (a) **alienate** any material assets whether by way of sale, lease, encumbrance or otherwise or enter into any agreement therefor outside the ordinary course of business;
 - (b) **effect any material borrowings** outside the ordinary course of business;
 - (c) **issue or allot** any authorised but unissued securities **entitling the holder to voting rights**:

Provided that the target company or its subsidiaries may,—

 - (i) **issue or allot shares upon conversion of convertible securities** issued prior to the public announcement of the open offer, in accordance with pre-determined terms of such conversion;
 - (ii) **issue or allot shares pursuant to any public issue** in respect of which the red herring prospectus has been filed with the Registrar of Companies prior to the public announcement of the open offer; or
 - (iii) **issue or allot shares pursuant to any rights issue** in respect of which the record date has been announced prior to the public announcement of the open offer;
 - (d) **implement any buy-back of shares** or **effect any other change to the capital structure** of the target company;
 - (e) **enter into, amend or terminate any material contracts** to which the target company or any of its subsidiaries is a party, outside the ordinary course of business, whether such contract is with a related party, within the meaning of the term under applicable accounting principles, or with any other person; and
 - (f) **accelerate any contingent vesting of a right of any person** to whom the target company or any of its subsidiaries may have an obligation, whether such obligation is to acquire shares of the target company by way of employee stock options or otherwise.
- (3) **Voting by target and its subsidiaries:** In any general meeting of a subsidiary of the target company in respect of the matters referred to in sub-regulation (2), the target company and its subsidiaries, if any, shall vote in a manner consistent with the special resolution passed by the shareholders of the target company.

- (4) **Prohibition from fixing record date:** The target company shall be prohibited from fixing any record date for a corporate action on or after the third working day prior to the commencement of the ¹¹tendering period and until the expiry of the tendering period.
- (5) **Furnishing of list of shareholders:** The target company shall furnish to the acquirer within two working days from the ¹²identified date, a list of shareholders as per the register of members of the target company containing names, addresses, shareholding and folio number, in electronic form, wherever available, and a list of persons whose applications, if any, for registration of transfer of shares are pending with the target company:

Provided that the acquirer shall reimburse reasonable costs payable by the target company to external agencies in order to furnish such information.

- (6) **Constitution of a committee of independent directors:** Upon receipt of the detailed public statement, the board of directors of the target company shall constitute a committee of independent directors to provide reasoned recommendations on such open offer, and the target company shall publish such recommendations:

Provided that such committee shall be entitled to seek external professional advice at the expense of the target company.

Provided further that while providing reasoned recommendations on the open offer proposal, the committee shall disclose the voting pattern of the meeting in which the open offer proposal was discussed.

- (7) **Duties of committee of independent directors:** The committee of independent directors shall provide its written reasoned recommendations on the open offer to the shareholders of the target company and such recommendations shall be published in such form as may be specified, at least two working days before the commencement of the tendering period, in the same newspapers where the public announcement of the open offer was published, and simultaneously, a copy of the same shall be sent to,—

¹¹ The term 'tendering period' refers to the 10 working days period falling within the offer period, during which the eligible shareholders who wish to accept the open offer can tender their shares in the open offer.

¹² Identified date means the date 10 working days prior to the commencement of the tendering period, for the purposes of determining the shareholders of the target company to whom the letter of offer along with the form of acceptance shall be sent.

the Board;

all the stock exchanges-

- on which the shares of the target company are listed, and
- the stock exchanges shall forthwith disseminate such information to the public; and

to the manager to the open offer, and

where there are competing offers, to the manager to the open offer for every competing offer.

- (8) **Verification of shares:** The board of directors of the target company shall facilitate the acquirer in verification of shares tendered in acceptance of the open offer.
- (9) **Providing of information and cooperation to acquirers:** The board of directors of the target company shall make available to all acquirers making competing offers, any information and co-operation provided to any acquirer who has made a competing offer.
- (10) **Register of transfer of shares:** Upon fulfillment by the acquirer, of the conditions required under these regulations, the board of directors of the target company shall without any delay register the transfer of shares acquired by the acquirer in physical form, whether under the agreement or from open market purchases, or pursuant to the open offer.

(iv) Obligations of the manager to the open offer (Regulation 27)

- (1) Prior to public announcement being made, **the manager to the open offer** shall ensure that,—
 - (a) the acquirer **is able to implement** the open offer; and
 - (b) **firm arrangements for funds** through verifiable means have been made by the acquirer to meet the payment obligations under the open offer.
- (2) The manager to the open offer **shall ensure that the contents** of the public announcement, the detailed public statement and the letter of offer and the post offer advertisement **are true, fair and adequate in all material aspects**, not misleading in any material particular, are based on reliable sources, state the source wherever necessary, and are in compliance with the requirements under these regulations.
- (3) The manager to the open offer shall **furnish to the Board a due diligence certificate** along with the draft letter of offer filed under regulation 16.
- (4) The manager to the open offer shall **ensure that market intermediaries** engaged for the purposes of the open offer **are registered** with the Board.

- (5) The manager to the open offer **shall exercise diligence, care and professional judgment** to ensure compliance with these regulations.
- (6) The manager to the open offer **shall not deal on his own account** in the shares of the target company during the offer period.
- (7) The manager to the open offer **shall file a report with the Board** within fifteen working days from the expiry of the tendering period, in such form as may be specified, confirming status of completion of various open offer requirements.

DISCLOSURES OF SHAREHOLDING AND CONTROL

Disclosure-related provisions (Regulation 28)

What all to be included under the disclosures? The disclosures shall be of the aggregated shareholding and voting rights of the acquirer or promoter of the target company or every person acting in concert with him. The acquisition and holding of any convertible security shall also be regarded as shares, and disclosures of such acquisitions and holdings shall be made accordingly. Upon receipt of the disclosures, the stock exchange shall forthwith disseminate the information so received.

For the purposes of this Chapter, the term “**encumbrance**” shall include,-

- (a) any restriction on the free and marketable title to shares, by whatever name called, whether executed directly or indirectly;
- (b) pledge, lien, negative lien, non-disposal undertaking; or
- (c) any covenant, transaction, condition or arrangement in the nature of encumbrance, by whatever name called, whether executed directly or indirectly.

Disclosure of acquisition and disposal (Regulation 29)

- (1) **Threshold for disclosures:** Any acquirer, together with persons acting in concert with him acquiring shares or voting rights in a target company, which taken together aggregates to **five per cent or more of the shares of such target company**, shall disclose their aggregate shareholding and voting rights in such target company in such form as may be specified

Provided that in case of **listed entity** which has listed its specified securities on Innovators Growth Platform, any reference to “**five per cent**” shall be read as “**ten per cent**”.

- (2) **In case of change in shareholding and voting rights:** Any person together with persons acting in concert with him, holds shares or voting rights entitling them to five per cent or more of the shares or voting rights in a target company, shall disclose the number of shares or voting rights held and **change in shareholding or voting rights**, even if such change results in shareholding falling below five per cent, if there has been change in such holdings from the last disclosure made as above or as given here, and such change exceeds two per cent of total shareholding or voting rights in the target company, in such form as may be specified.

Provided that in case of **listed entity** which has listed its specified securities on Innovators Growth Platform, any reference to “five per cent” shall be read as “ten per cent” and any reference to “two per cent” shall be read as “five per cent”.

- (3) **Period of disclosures:** The disclosures required shall be made within two working days of the receipt of intimation of allotment of shares, or the acquisition or the disposal of shares or voting rights in the target company to,—

- (a) every stock exchange where the shares of the target company are listed; and
- (b) the target company at its registered office.

- (4) **Shares taken by way of encumbrance** shall be treated as an acquisition, shares given upon release of encumbrance shall be treated as a disposal, and disclosures shall be made by such person accordingly in such form as may be specified:

Exempted: Provided that such requirement shall not apply to a scheduled commercial bank or public financial institution or a housing finance company or a systemically important non-banking financial company as pledgee in connection with a pledge of shares for securing indebtedness in the ordinary course of business.

Explanation - For the purpose of this sub-regulation -

- A. a “**housing finance company**” means a housing finance company registered with the National Housing Bank for carrying on the business of housing finance and is either deposit taking or having asset size worth rupees five hundred crores or more; and
- B. a “**systemically important non-banking financial company**” shall have the same meaning as assigned to it in the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018.

Disclosure of encumbered shares (Regulation 31)

- (1) **Disclosure of share’s details by promoter:** The promoter of every target company shall disclose details of shares in such target company encumbered by him or by persons acting in concert with him in such form as may be specified:

Provided that the aforesaid disclosure requirement shall not be applicable where such encumbrance is undertaken in a depository.

- (2) **Details of invocation:** The promoter of every target company shall disclose details of any invocation of such encumbrance or release of such encumbrance of shares in such form as may be specified:

Provided that the aforesaid disclosure requirement shall not be applicable where such encumbrance is undertaken in a depository.

- (3) **Time period of disclosure:** The disclosures required under sub-regulation (1) and sub-regulation (2) shall be made within seven working days from the creation or invocation or release of encumbrance, as the case may be to,—
- every stock exchange where the shares of the target company are listed; and
 - the target company at its registered office.
- (4) **Declaration of not made any encumbrance:** The promoter of every target company shall declare on a yearly basis that he, along with persons acting in concert, has not made any encumbrance, directly or indirectly, other than those already disclosed during the financial year.
- (5) **Time period of declaration:** The declaration required under sub-regulation (4) shall be made within seven working days from the end of each financial year to –
- every stock exchange where the shares of the target company are listed; and
 - the audit committee of the target company.

Accordingly as per the regulation, the promoter (along with PACs) of the target company shall disclose details of shares encumbered by them or any invocation or release of encumbrance of shares held by them to the target company at its registered office and every stock exchange where shares of the target company are listed, within 7 working days of such event. Further, promoter also has to declare on a yearly basis that he along with persons acting in concert has not made any encumbrance other than those already disclosed during the financial year.

An **illustrative example** is as follows:

- If the promoter has encumbered shares on January 01, 2020 and as a result the encumbrance of promoter along with PACs increases from NIL to 60% of their shareholding, the promoter has to disclose detailed reasons for encumbrance.
- Subsequently, if the promoter once again encumbers additional shares on February 01, 2020 and as a result the encumbrance of promoter along with PACs increases from 60% to 65% of their shareholding, the promoter has to again disclose detailed reasons for encumbrance

SECURITIES AND EXCHANGE BOARD OF INDIA (PROHIBITION OF INSIDER TRADING) REGULATIONS, 2015

Insider trading essentially denotes dealing in a company's securities on the basis of confidential information, relating to the company, which is not published or not known to the public (known as 'unpublished price sensitive information'), used to make personal profits or avoid loss.

In exercise of the powers conferred by section 30 read with clause (g) of sub-section (2) of section 11 and clause (d) and clause (e) of section 12A of the Securities and Exchange Board of India Act, 1992, SEBI vide Gazette notification no. LADNRO/GN/2014-15/21/85 dated 15th January 2015 had notified the SEBI (Prohibition of Insider Trading) Regulations, 2015 to put in place a framework for

prohibition of insider trading in securities and to strengthen the legal framework thereof. The regulations came into effect from May 15th, 2015 and has been amended from time to time.

DEFINITIONS [Regulation 2(1)]

Insider: Regulation 2(1) (g) of SEBI (PIT) Regulations, 2015 defines 'insider' as any person who is:

- (i) a connected person; or
- (ii) in possession of or having access to unpublished price sensitive information.

Whereas "**connected person**" means,-

- (i) **any person-**
 - who is or has during the **six months prior to the concerned act been associated with a company**, directly or indirectly,
 - **in any capacity** including by reason of frequent communication with its officers or by being in any contractual, fiduciary or employment relationship or by being a director, officer or an employee of the company or holds any position including a professional or business relationship between himself and the company whether temporary or permanent,
 - that **allows such person**, directly or indirectly, **access to unpublished price sensitive information** or is reasonably expected to **allow such access**.
- (ii) the persons falling within the **following categories** shall be deemed to be connected persons, -
 - (a) an ¹³**immediate relative of connected persons** specified in clause (i); or
 - (b) a **holding company or associate company or subsidiary company**; or
 - (c) an **intermediary** as specified in section 12 of the Act or an **employee or director** thereof; or
 - (d) an **investment company, trustee company, asset management company** or an **employee or director** thereof; or
 - (e) an **official of a stock exchange or of clearing house or corporation**; or
 - (f) a **member of board of trustees** of a mutual fund or a **member of the board of directors** of the asset management company of a mutual fund or is an **employee** thereof; or
 - (g) a **member of the board of directors** or an **employee, of a public financial institution** as defined in section 2 (72) of the Companies Act, 2013; or
 - (h) an **official or an employee of a self-regulatory organization** recognised or authorized by the Board; or

¹³ means a spouse of a person, and includes parent, sibling, and child of such person or of the spouse, any of whom is either dependent financially on such person, or consults such person in taking decisions relating to trading in securities;

- (i) a banker of the company; or
- (j) a concern, firm, trust, Hindu undivided family, company or association of persons wherein a director of a company or his immediate relative or banker of the company, has more than **ten per cent. of the holding or interest**;

It is to be noted that the above definition intends to bring into its ambit persons who may not seemingly occupy any position in a company but are in regular touch with the company and its officers and are involved in the know of the company's operations.

According to Regulation 2(1) clause (e) "**generally available information**" is defined as information that is accessible to the public on a non-discriminatory basis. It is intended that anyone in possession of or having access to unpublished price sensitive information should be considered an "insider" regardless of how one came in possession of or had access to such information. Therefore, this definition is intended to bring within its reach any person who is in receipt of or has access to unpublished price sensitive information.

Any information published on the website of a stock exchange, would ordinarily be considered generally available.

"Unpublished price sensitive information (UPSI)" as per Regulation 2(1) (n) of SEBI (PIT) Regulations, 2015, means any information, relating to a company or its securities, directly or indirectly, that is not generally available which upon becoming generally available, is likely to materially affect the price of the securities and shall, ordinarily including but not restricted to, information relating to the following: –

- i) financial results;
- ii) dividends;
- iii) change in capital structure;
- iv) mergers, de-mergers, acquisitions, delistings, disposals and expansion of business and such other transactions;
- v) changes in key managerial personnel.

Law intended that information relating to a company or securities that is not generally available would be unpublished price sensitive information if it is likely to materially affect the price upon coming into the public domain. The types of matters that would ordinarily give rise to unpublished price sensitive information have been listed above to give illustrative guidance of unpublished price sensitive information.

"Trading- Regulation 2(1) (l) of SEBI (PIT) Regulations, 2015, means and includes subscribing, redeeming, switching, buying, selling, dealing, or agreeing to subscribe, redeem, switch, buy, sell, deal in any securities, and "trade" shall be construed accordingly.

"Trading day" means a day on which the recognized stock exchanges are open for trading [Regulation 2(1)(m)]

RESTRICTIONS ON COMMUNICATION AND TRADING BY INSIDERS**Communication or procurement of unpublished price sensitive information (UPSI) (Regulation 3)**

- (1) No insider shall **communicate, provide, or allow access** to any unpublished price sensitive information, **relating to a company or securities** listed or proposed to be listed, **to any person** including other insiders, **except** where such communication is in furtherance of legitimate purposes, performance of duties or discharge of legal obligations.

This provision is intended to cast an obligation on all insiders who are essentially persons in possession of unpublished price sensitive information to handle such information with care and to deal with the information with them when transacting their business strictly on a need-to-know basis.

- (2) No person shall **procure from or cause the communication by any insider** of unpublished price sensitive information, **relating to a company or securities** listed or proposed to be listed, **except** in furtherance of legitimate purposes, performance of duties or discharge of legal obligations.

This provision is intended to impose a prohibition on unlawfully acquiring possession of unpublished price sensitive information. Inducement and procurement of unpublished price sensitive information not in furtherance of one's legitimate duties and discharge of obligations would be illegal under this provision.

- (2A) The **board of directors** of a listed company **shall make a policy for determination of "legitimate purposes"** as a part of "Codes of Fair Disclosure and Conduct" formulated under regulation 8.

Explanation – For the purpose of illustration, the term "**legitimate purpose**" shall include sharing of unpublished price sensitive information in the ordinary course of business by an insider with partners, collaborators, lenders, customers, suppliers, merchant bankers, legal advisors, auditors, insolvency professionals or other advisors or consultants, provided that such sharing has not been carried out to evade or circumvent the prohibitions of these regulations.

- (2B) Any **person in receipt of unpublished price sensitive information** pursuant to a "legitimate purpose" shall be considered an "insider" for purposes of these regulations and due notice shall be given to such persons to maintain confidentiality of such unpublished price sensitive information in compliance with these regulations.

- (3) **Communication of UPSI:** An unpublished price sensitive information may be communicated, provided, allowed access to or procured, in connection with a transaction that would:–

- (i) **entail an obligation to make an open offer** under the takeover regulations where the board of directors of the listed company is of informed opinion that sharing of such information is in the best interests of the company;

Law intends to acknowledge the necessity of communicating, providing, allowing access to or procuring UPSI for substantial transactions such as takeovers, mergers and

acquisitions involving trading in securities and change of control to assess a potential investment. In an open offer under the takeover regulations, not only would the same price be made available to all shareholders of the company but also all information necessary to enable an informed divestment or retention decision by the public shareholders is required to be made available to all shareholders in the letter of offer under those regulations.

- (ii) **not attract the obligation to make an open offer** under the takeover regulations but where the board of directors of the listed company is of informed opinion that sharing of such information is in the best interests of the company and the information that constitute unpublished price sensitive information is disseminated to be made generally available at least two trading days prior to the proposed transaction being effected in such form as the board of directors may determine to be adequate and fair to cover all relevant and material facts.

Said provision is intended to permit communicating, providing, allowing access to or procuring UPSI also in transactions that do not entail an open offer obligation under the takeover regulations when authorised by the board of directors if sharing of such information is in the best interests of the company. The board of directors, however, would cause public disclosures of such unpublished price sensitive information well before the proposed transaction to rule out any information asymmetry in the market.

- (4) For Communication of UPSI, the board of directors shall require the parties **to execute agreements** to contract confidentiality and non-disclosure obligations on the part of such parties and such parties shall keep information so received confidential, except for the purpose of sub-regulation (3), and shall not otherwise trade in securities of the company when in possession of unpublished price sensitive information.
- (5) The Board of Directors or head(s) of the organisation of every person required to handle unpublished price sensitive information shall ensure that a **structured digital database is maintained** containing the nature of unpublished price sensitive information and the names of such persons who have shared the information and also the names of such persons with whom information is shared under this regulation along with the Permanent Account Number or any other identifier authorized by law where Permanent Account Number is not available. Such database shall not be outsourced and shall be maintained internally with adequate internal controls and checks such as time stamping and audit trails to ensure non-tampering of the database.

Structured Digital Database:

- The requirement to maintain Structured Digital Database is applicable to **Listed Companies, and Intermediaries and Fiduciaries** who handle UPSI of a Listed Company in the course of business operations.
 - The Listed Company in its database **shall record nature of UPSI shared, details of the Sender and Receiver** (both Individual and Entity recipient) along with their PAN or other unique identifier (in case PAN is not available).
 - The **Intermediary / Fiduciary** in its database shall record nature of UPSI received/shared, details of the Company whose UPSI is received/shared, details of individual Sender and Receiver along with their PAN or other unique identifier (in case PAN is not available).
 - **Databases/servers provided by third party vendors** whether within India or outside India will be considered as outsourced.
 - **Records shall be updated in Structured Digital Database as and when the information gets transmitted** (irrespective of the fact that information is shared within or outside the Company).
- (6) The board of directors or head(s) of the organisation of every person required to handle unpublished price sensitive information shall ensure that the **structured digital database is preserved for a period of not less than eight years after completion of the relevant transactions** and in the event of receipt of any information from the Board regarding any investigation or enforcement proceedings, the relevant information in the structured digital database shall be preserved till the completion of such proceedings.

Trading when in possession of unpublished price sensitive information (Regulation 4)

- (1) **No insider shall trade in securities** that are listed or proposed to be listed on a stock exchange when in possession of unpublished price sensitive information:

Explanation –When a person who has traded in securities has been in possession of unpublished price sensitive information, his trades would be presumed to have been motivated by the knowledge and awareness of such information in his possession.

Provided that the **insider may prove his innocence** by demonstrating the circumstances including the following: –

- (i) the **transaction is an off-market inter-se transfer** between insiders who were in possession of the same unpublished price sensitive information without being in breach of regulation 3 and both parties had made a conscious and informed trade decision.

Exception: Provided that such unpublished price sensitive information was not obtained under sub-regulation (3) of regulation 3 of these regulations.

Reporting of off-market trades: Provided further that such off-market trades shall be reported by the insiders to the company within two working days. Every company shall notify the particulars of such trades to the stock exchange on which the securities are listed within two trading days from receipt of the disclosure or from becoming aware of such information.

- (ii) the **transaction was carried out through the block deal window mechanism** between persons who were in possession of the unpublished price sensitive information without being in breach of regulation 3 and both parties had made a conscious and informed trade decision;

Provided that such unpublished price sensitive information was not obtained by either person under sub-regulation (3) of regulation 3 of these regulations.

- (iii) the transaction in question was **carried out pursuant to a statutory or regulatory obligation** to carry out a bona fide transaction.
- (iv) the transaction in question was undertaken **pursuant to the exercise of stock options in respect of which the exercise price was pre-determined** in compliance with applicable regulations.
- (v) in the case of **non-individual insiders**: –
 - (a) the individuals who were in possession of such unpublished price sensitive information were different from the individuals taking trading decisions and such decision-making individuals were not in possession of such unpublished price sensitive information when they took the decision to trade; and
 - (b) appropriate and adequate arrangements were in place to ensure that these regulations are not violated and no unpublished price sensitive information was communicated by the individuals possessing the information to the individuals taking trading decisions and there is no evidence of such arrangements having been breached;
- (vi) the **trades were pursuant to a trading plan** set up in accordance with regulation 5.

When a person who has traded in securities has been in possession of unpublished price sensitive information, his trades would be presumed to have been motivated by the knowledge and awareness of such information in his possession. The reasons for which he trades or the purposes to which he applies the proceeds of the transactions are not intended to be relevant for determining whether a person has violated the regulation. He traded when in possession of unpublished price sensitive information is what would need to be demonstrated at the outset to bring a charge. Once this is established, it would be open to the insider to prove his innocence by demonstrating the circumstances mentioned in the proviso, failing which he would have violated the prohibition.

- (2) **Onus of possessing UPSI:** In the case of connected persons the onus of establishing, that they were not in possession of unpublished price sensitive information, shall be on such connected persons and in other cases, the onus would be on the Board.
- (3) The **Board may specify such standards and requirements**, from time to time, as it may deem necessary for the purpose of these regulations.

Trading Plans (Regulation 5)

- (1) **Formulation of trade plan:** An insider shall be entitled to formulate a trading plan and present it to the compliance officer for approval and public disclosure pursuant to which trades may be carried out on his behalf in accordance with such plan.

This provision intends to give an option to persons who may be perpetually in possession of unpublished price sensitive information and enabling them to trade in securities in a compliant manner. This provision would enable the formulation of a trading plan by an insider to enable him to plan for trades to be executed in future. By doing so, the possession of unpublished price sensitive information when a trade under a trading plan is actually executed would not prohibit the execution of such trades that he had pre-decided even before the unpublished price sensitive information came into being.

Trading as per Trading Plan can be done if in any case UPSI which was in existence at the time of formulation of such Plan has been made generally available. In case the UPSI is not generally available, then no trading shall be done.

If at the time of formulation of trading plan, there was no UPSI or later on a new UPSI was generated, then the trading can be carried out as per the trading plan, even if the new UPSI has not been made generally available.

- (2) Such **trading plan** shall:–
 - (i) **not entail commencement of trading** on behalf of the insider earlier than six months from the public disclosure of the plan;

It is intended that to get the benefit of a trading plan, a cool-off period of six months is necessary. Such a period is considered reasonably long for unpublished price sensitive information that is in possession of the insider when formulating the trading plan, to become generally available. It is also considered to be a reasonable period for a time lag in which new unpublished price sensitive information may come into being without adversely affecting the trading plan formulated earlier. In any case, it should be remembered that this is only a statutory cool-off period and would not grant immunity from action if the insider were to be in possession of the same unpublished price sensitive information both at the time of formulation of the plan and implementation of the same.

- (ii) **not entail trading for the period between the twentieth trading day prior to the last day of any financial period** for which results are required to be announced by the issuer of the securities and the second trading day after the disclosure of such financial results;

Since the trading plan is envisaged to be an exception to the general rule prohibiting trading by insiders when in possession of unpublished price sensitive information, it is important that the trading plan does not entail trading for a reasonable period around the declaration of financial results as that would generate unpublished price sensitive information.

- (iii) **entail trading for a period of not less than twelve months ;**

It is intended that it would be undesirable to have frequent announcements of trading plans for short periods of time rendering meaningless the defence of a reasonable time gap between the decision to trade and the actual trade. Hence it is felt that a reasonable time would be twelve months.

- (iv) **not entail overlap of any period** for which another trading plan is already in existence;

It is intended that it would be undesirable to have multiple trading plans operating during the same time period. Since it would be possible for an insider to time the publication of the unpublished price sensitive information to make it generally available instead of timing the trades, it is important not to have the ability to initiate more than one plan covering the same time period.

- (v) **set out either the value of trades** to be effected or the **number of securities** to be traded along with the nature of the trade and the intervals at, or dates on which such trades shall be effected; and

It is intended that while regulations should not be too prescriptive and rigid about what a trading plan should entail, they should stipulate certain basic parameters that a trading plan should conform to and within which, the plan may be formulated with full flexibility. The nature of the trades entailed in the trading plan i.e. acquisition or disposal should be set out. The trading plan may set out the value of securities or the number of securities to be invested or divested. Specific dates or specific time intervals may be set out in the plan.

- (vi) **not entail trading in securities** for market abuse.

Trading on the basis of such a trading plan would not grant absolute immunity from bringing proceedings for market abuse. For instance, in the event of manipulative timing of the release of unpublished price sensitive information to ensure that trading under a trading plan becomes lucrative in circumvention of regulation 4 being detected, it would be open to initiate proceedings for alleged breach of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to the Securities Market) Regulations, 2003.

- (3) The compliance officer shall **review the trading plan** to assess whether the plan would have any potential for violation of these regulations and shall be entitled to seek such express undertakings

as may be necessary to enable such assessment and to approve and monitor the implementation of the plan.

Provided that pre-clearance of trades shall not be required for a trade executed as per an approved trading plan.

Provided further that trading window norms and restrictions on contra trade shall not be applicable for trades carried out in accordance with an approved trading plan.

It is intended that the compliance officer would have to review and approve the plan. For doing so, he may need the insider to declare that he is not in possession of unpublished price sensitive information or that he would ensure that any unpublished price sensitive information in his possession becomes generally available before he commences executing his trades. Once satisfied, he may approve the trading plan, which would then have to be implemented in accordance with these regulations.

- (4) The **trading plan once approved shall be irrevocable** and the insider shall mandatorily have to implement the plan, without being entitled to either deviate from it or to execute any trade in the securities outside the scope of the trading plan.

Provided that the implementation of the trading plan shall not be commenced if any unpublished price sensitive information in possession of the insider at the time of formulation of the plan has not become generally available at the time of the commencement of implementation and in such event the compliance officer shall confirm that the commencement ought to be deferred until such unpublished price sensitive information becomes generally available information so as to avoid a violation of sub-regulation (1) of regulation 4.

It is intended that since the trading plan is an exception to the general rule that an insider should not trade when in possession of unpublished price sensitive information, changing the plan or trading outside the same would negate the intent behind the exception. Other investors in the market, too, would factor the impact of the trading plan on their own trading decisions and in price discovery. Therefore, it is not fair or desirable to permit the insider to deviate from the trading plan based on which others in the market have assessed their views on the securities.

The proviso is intended to address the prospect that despite the six-month gap between the formulation of the trading plan and its commencement, the unpublished price sensitive information in possession of the insider is still not generally available. In such a situation, commencement of the plan would conflict with the over-riding principle that trades should not be executed when in possession of such information. If the very same unpublished price sensitive information is still in the insider's possession, the commencement of execution of the trading plan ought to be deferred.

- (5) **Upon approval of the trading plan**, the compliance officer shall notify the plan to the stock exchanges on which the securities are listed.

It is intended that given the material exception to the prohibitory rule in regulation 4, a trading plan is required to be publicly disseminated. Investors in the market at large would also factor the potential pointers in the trading plan in their own assessment of the securities and price discovery for them on the premise of how the insiders perceive the prospects or approach the securities in their trading plan.

DISCLOSURES OF TRADING BY INSIDERS

General provisions (Regulation 6)

- (1) How disclosure shall be made? Every public disclosure under this Chapter shall be made in such form as may be specified.
- (2) Who can make disclosure? The disclosures to be made **by any person** under this Chapter shall include those relating to trading by such person's immediate relatives, and by any other person for whom such person takes trading decisions.

It is intended that disclosure of trades would need to be of not only those executed by the person concerned but also by the **immediate relatives** and **of other persons** for whom the person concerned takes trading decisions. These regulations are primarily aimed at preventing abuse by trading when in possession of unpublished price sensitive information and therefore, what matters is whether the person who takes trading decisions is in possession of such information rather than whether the person who has title to the trades is in such possession.

- (3) The disclosures of trading in securities shall also **include trading in derivatives of securities and the traded value of the derivatives** shall be taken into account for purposes of this Chapter:

Provided that trading in derivatives of securities is permitted by any law for the time being in force.

The disclosures made under this Chapter shall be **maintained by the company, for a minimum period of five years**, in such form as may be specified.

Disclosures by certain persons (Regulation 7)

- (1) **Initial Disclosures**

Every person on appointment as a key managerial personnel or a director of the company or upon becoming a promoter or member of the promoter group- shall disclose his holding of securities of the company as on the date of appointment or becoming a promoter, to the company within seven days of such appointment or becoming a promoter.

- (2) **Continual Disclosures**

- (a) Every promoter, member of the promoter group, designated person and director of every company shall disclose to the company the number of such securities acquired

or disposed of within two trading days of such transaction if the value of the securities traded, whether in one transaction or a series of transactions over any calendar quarter, aggregates to a traded value in excess of ten lakh rupees or such other value as may be specified;

- (b) Every **company shall notify the particulars of such trading to the stock exchange** on which the Securities are listed **within two trading days** of receipt of the disclosure or from becoming aware of such information.

Explanation — It is clarified for the avoidance of doubts that the disclosure of the incremental transactions after any disclosure under this sub-regulation, shall be made when the transactions effected after the prior disclosure cross the threshold specified in clause (a) of sub-regulation (2).

- (c) **Time for disclosures:** The above disclosures shall be made in such form and such manner as may be specified by the Board from time to time.
- Upon filing of a disclosure under Regulation 7(2)(b) of SEBI Regulations, the disclosure of the incremental transactions after any disclosure shall be made when the transactions effected after the prior disclosure cross the threshold specified in Clause (a) of Sub-Regulation (2) of Regulation 7. Hence, the next disclosure will be due when the next Rs. 10 lacs limit is breached.
 - For filing of disclosures, the market rate of the trades shall be considered for calculating the threshold limit. The market price shall not be subtracted by subtracting Brokerage, Commission etc. i.e.net of taxes and all transaction charges.
 - The disclosure shall be filed irrespective of what the mode of acquisition is except for the shares acquired via bonus issue or received pursuant to a Scheme

Disclosures by other connected persons

Any company whose securities are listed on a stock exchange may, at its discretion require any other connected person or class of connected persons to make disclosures of holdings and trading in securities of the company in such form and at such frequency as may be determined by the company in order to monitor compliance with these regulations.

This is an enabling provision for listed companies to seek information from those to whom it has to provide unpublished price sensitive information. This provision confers discretion on any company to seek such information. For example, a listed company may ask that a management consultant who would advise it on corporate strategy and would need to review unpublished price sensitive information, should make disclosures of his trades to the company.

Chapter IIIA has been added to SEBI (Prohibition of Insider Trading) Regulations 2015 vide SEBI (Prohibition of Insider Trading (Third Amendment) Regulations, 2019 w.e.f December 26, 2019,

prescribing for incentive and reward for the informants who submits to the SEBI a Voluntary Information Disclosure relating to any alleged violation of insider trading laws that has occurred, in occurring or has a reasonable belief that it is about to occur. The new provisions prescribe the manner of submitting information, various forms and procedure for determination of rewards and confidentiality of informants.

Brief process flow of submission to the SEBI [Regulation 7 (B)]

An Informant shall submit **Original Information in Voluntary Information Disclosure Form to the Office of Informant Protection** of the SEBI.

The format and manner of the Form shall be as set out in **Schedule D** and may be submitted by a **legal representative** of the Informant.

If the Informant does not submit the Form through a legal representative SEBI may require the **informant to appear in person** to ascertain his/her identity & veracity of the information.

The Informant while submitting the Voluntary Information Disclosure Form shall **expunge the information** in the Form which could reasonably be expected to reveal his/her identity.

If expunging the information is not possible the Informant may **identify such information /document** that he believes could reasonably be expected to reveal his/her identity.

CODES

Chapter IV of SEBI (Prohibition of Insider Trading) Regulations 2015 deals with codes to be documented and followed by listed companies/market intermediaries

Code of Fair Disclosure

Regulation 8 (1) states that the board of directors of every company, whose securities are listed on a stock exchange, shall formulate and publish on its official website, a code of practices and procedures for fair disclosure of unpublished price sensitive information that it would follow in order to adhere to each of the principles set out in Schedule A to these regulations, without diluting the provisions of these regulations in any manner.

To notify the code of fair disclosure/amendment thereof to the stock exchanges.

Regulation 8(2) states that every such code of practices and procedures for fair disclosure of unpublished price sensitive information and every amendment thereto shall be promptly intimated to the stock exchanges where the securities are listed.

The board of directors of a listed company shall make a policy for determination of “legitimate purposes” as a part of “Codes of Fair Disclosure and Conduct” formulated under regulation 8.

The term “legitimate purpose” shall include sharing of unpublished price sensitive information in the ordinary course of business by an insider with partners, collaborators, lenders, customers, suppliers, merchant bankers, legal advisors, auditors, insolvency professionals or other advisors or

consultants, provided that such sharing has not been carried out to evade or circumvent the prohibitions of these regulations.

Code of Conduct

Regulation 9 (1) states that the board of directors of every listed company and the board of directors or head(s) of the organisation of every intermediary shall ensure that the chief executive officer or managing director shall formulate a code of conduct with their approval to regulate, monitor and report trading by its designated persons and immediate relatives of designated persons towards achieving compliance with these regulations, adopting the minimum standards set out in Schedule B (in case of a listed company) and Schedule C (in case of an intermediary) to these regulations, without diluting the provisions of these regulations in any manner.

Explanation – For the avoidance of doubt it is clarified that intermediaries, which are listed, would be required to formulate a code of conduct to regulate, monitor and report trading by their designated persons, by adopting the minimum standards set out in Schedule B with respect to trading in their own securities and in Schedule C with respect to trading in other securities.

Regulation 9 (2) states the board of directors or head(s) of the organisation, of every other person who is required to handle unpublished price sensitive information in the course of business operations shall formulate a code of conduct to regulate, monitor and report trading by their designated persons and immediate relative of designated persons towards achieving compliance with these regulations, adopting the minimum standards set out in Schedule C to these regulations, without diluting the provisions of these regulations in any manner.

Explanation - Professional firms such as auditors, accountancy firms, law firms, analysts, insolvency professional entities, consultants, banks etc., assisting or advising listed companies shall be collectively referred to as fiduciaries for the purpose of these regulations.

Every listed company, intermediary and other persons formulating a code of conduct shall identify and designate a compliance officer to administer the code of conduct and other requirements under these regulations.

The board of directors or such other analogous authority shall in consultation with the compliance officer specify the **designated persons** to be covered by the code of conduct on the basis of their role and function in the organisation and the access that such role and function would provide to unpublished price sensitive information in addition to seniority and professional designation and **shall include:-**

- (i) Employees of such listed company, intermediary or fiduciary designated on the basis of their functional role or access to unpublished price sensitive information in the organization by their board of directors or analogous body;
- (ii) Employees of material subsidiaries of such listed companies designated on the basis of their functional role or access to unpublished price sensitive information in the organization by their board of directors;

- (iii) All promoters of listed companies and promoters who are individuals or investment companies for intermediaries or fiduciaries;

Penalty for insider trading under section 15G of the SEBI Act, 1992

If any insider who-

- (i) either on his own behalf or on behalf of any other person, deals in securities of a body corporate listed on any stock exchange on the basis of any unpublished price sensitive information; or
- (ii) communicates any unpublished price sensitive information to any person, with or without his request for such information except as required in the ordinary course of business or under any law; or
- (iii) counsels, or procures for any other person to deal in any securities of any body corporate on the basis of unpublished price sensitive information,

shall be liable to a penalty which shall not be less than ten lakh rupees but which may extend to twenty-five crore rupees or three times the amount of profits made out of insider trading, whichever is higher.

TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. *Aayush, Bipin, Carroll & Co., a firm of Chartered Accountants, was appointed as statutory auditor of Ruchika Flavours Limited, a listed company, for the financial year 2019-20. Mr. Bipin is the engaging partner of the said audit with a team of fifteen members. While conducting audit of the financial statements of Ruchika Flavours Limited, two members of Mr. Bipin's team, who are Chartered Accountants, passed the information to their friends and relatives disclosing that the profits of Ruchika Flavours Limited for this year are increasing by 25% in comparison to the previous audited financial year. At the time of passing the information, it was not available in the public domain through the company. Certain persons who were in possession of this information, purchased the shares of Ruchika Flavours Limited at a low price. After the audited financial statements came into public domain, the market price of the shares increased sharply and they made profit by selling the shares, earlier purchased at low price, at the enhanced market price. You are required to select the correct option which indicates whether it is a case of insider trading or not and if it is a case of insider trading then the quantum of penalty that can be levied under the Securities and Exchange Board of India, Act, 1992.*
 - (a) *It is not a case of insider trading since both the Chartered Accountants are part of statutory audit team and therefore, are not restricted to use any information relating to Ruchika Flavours Limited.*
 - (b) *It is not a case of insider trading since the information disclosed by both the Chartered Accountants of statutory audit team is not a price-sensitive information.*
 - (c) *It is a case of insider trading and therefore, the penalty leviable would be not less than ₹ 10 lacs but which may extend to ₹ 25 crores or three times of profits made out of insider trading, whichever is higher.*
 - (d) *It is a case of insider trading and therefore, the penalty leviable would be not less than ₹ 25 crores or three times of profits made out of insider trading, whichever is lower.*
2. *Akshara Builders and Developers Ltd., a company listed on BSE Limited, is contemplating upper revision in the rate of interest of its existing 12% bonds by 1% so as to make them 13% bonds with effect from August 14, 2021. The said proposal is to be laid before the Board of Directors at a Board Meeting to be held on July 14, 2021. From the following options, choose the one which correctly indicates the latest date by which Akshara Builders and Developers Ltd. is required to intimate the BSE Limited about the Board Meeting where increase in rate of interest is being considered, keeping in view the Regulation 29 of Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015:*

- (a) Akshara Builders and Developers Ltd. is required to intimate BSE Limited about the Board Meeting, where increase in rate of interest is being considered, latest by July 1, 2021.
- (b) Akshara Builders and Developers Ltd. is required to intimate BSE Limited about the Board Meeting, where increase in rate of interest is being considered, latest by July 3, 2021.
- (c) Akshara Builders and Developers Ltd. is required to intimate BSE Limited about the Board Meeting, where increase in rate of interest is being considered, latest by July 5, 2021.
- (d) Akshara Builders and Developers Ltd. is required to intimate BSE Limited about the Board Meeting, where increase in rate of interest is being considered, latest by July 7, 2021.
3. W Ltd. made the following compliances for the June 2022 quarter, as required by SEBI(LODR) Regulations, 2015 :-
- 1) It submitted its unaudited quarterly financial statements to the recognised stock exchange on 31st July, 2022.
 - 2) It submitted its quarterly compliance report on corporate governance on 10th July, 2022.
- What shall be the last date of submission of quarterly financial statements to the stock exchange for W Ltd., in case W Ltd. was not able to submit the same on 31st July, 2022, and whether it can be submitted in unaudited form also?
- (a) 15th August, 2022 and no, it needs to be submitted in audited form.
 - (b) 31st August, 2022 and yes, it can be submitted in unaudited form.
 - (c) 31st July, 2022 and no, it needs to be submitted in audited form.
 - (d) 15th August, 2022 and yes, it can be submitted in unaudited form.
4. Mr. Amar is holding the post of directorship in following Listed entities- LE 1, LE 2, LE 3, LE 4, LE 5 LE 6, and LE 7 as on January 2020. He received an offer of directorship from LE 8 in April 2020. Whether Amar can join the LE 8?
- (a) Yes, as per the SEBI(LODR)Regulation, directorship is restricted to 8 listed entities. Hence Mr. Amar can.
 - (b) Yes, as per the SEBI(LODR)Regulation read with the companies Act, 2013, Mr. Amar can accept directorship in 10 listed companies.
 - (c) No, as per the SEBI(LODR)Regulation, directorship cannot be in more than seven listed entities with effect from April 1, 2020, Mr. Amar cannot.
 - (d) Yes, as no restriction is marked on holding of directorship in the Listed companies.

5. As per SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, no acquirer shall acquire shares or voting rights in a target company which taken together with shares or voting rights, if any, held by him and by persons acting in concert with him in such target company, entitle them to exercise ____ of the voting rights in such target company unless the acquirer makes a public announcement of an open offer for acquiring shares of such target company:
- (a) Ten percent or more
 - (b) Twenty per cent or more
 - (c) Twenty-five per cent or more
 - (d) Fifty per cent or more

Descriptive Questions

1. A group of complainants have alleged that Mr. Z, a Member of the Securities and Exchange Board of India (SEBI) has pecuniary interest in some of the cases that came up before the Board and that he misused his position and therefore, he should be removed from his office. The complainants seek your advice. Advise.
2. SEBI received complaints from some investors alleging that ABC Ltd. and some brokers are indulging in price manipulation in the shares of ABC Ltd. Explain the powers that can be exercised by SEBI under the Securities and Exchange Board of India Act, 1992 in case the allegations are found to be correct.
3. Clever who is registered as an Intermediary fails to enter into an agreement with his client and hence penalised by SEBI under section 15B of the SEBI Act. Advise Mr. Clever as to what remedies are available to him against the order of SEBI.
4. A group of investors are upset with the functioning of two leading stock brokers of Calcutta Stock Exchange and want to make a complaint to SEBI for intervention and redressal of their grievances. Explain briefly the purpose of establishing SEBI and what type of defaults by the stock brokers come within the purview of SEBI Act, 1992.
5. Mr. Raman, an investor is not satisfied with the dealings of his stock broker who is registered with Delhi Stock Exchange. Mr. Raman approaches you to guide him regarding the avenues available to him for making a complaint against the stock broker under Securities and Exchange Board of India Act, 1992 and also the grounds on which such complaint can be made. You are required to briefly explain the answer to his queries.
6. On the complaint of Mr. Kamlesh Gupta, after enquiry SEBI finds that Mr. P. Mehta, a Chief Executive Officer of the Company, on the basis of unpublished price sensitive information, has indulged in the trading of the securities of that company. Explain, on the basis of the said finding, what action SEBI can take against Mr. P. Mehta under the Securities and Exchange Board of India Act, 1992.

7. Securities and Exchange Board of India (SEBI) has undertaken inspection of books of accounts and records of LR Ltd., a listed public company. Specify the measures which may be taken by SEBI under the Securities and Exchange Board of India Act, 1992 to protect the interest of investors and securities market, on completion of such inquiry.
8. Mr. S, a member of MN Ltd., obtained an order from the Securities and Exchange Board of India (SEBI) against the company. But the company failed to redress the grievance of Mr. S within the time fixed. Consequently, SEBI imposed penalty on the company. The company, however, did not pay the penalty also. State how the penalty can be recovered from the company?
9. The composition of Audit Committee of M/s MKBTC Limited, an unlisted Public Company, as on 31-3-2019 comprised of 7 Directors including 4 Independent Directors. The majority of the members of the Audit Committee has the ability to read and understand the financial statements but none of them has accounting or related financial management expertise. The Company listed its Securities in a recognized Stock Exchange in the month of August 2019. Referring to the regulations of Securities and Exchange Board of India [Listing Obligations and Disclosure Requirements] Regulations 2015, decide whether the existing Audit Committee can continue after listing of its Securities?
10. Mr. Zubin (Member of SEBI) was adjudged as an insolvent by the Adjudicating authority. As of that, a group of complainants have alleged that Mr. Zubin while rendering of his services in office may be biased in the performance of his duties. Working in such a state of position by him, may be detrimental to the public interest and so should be removed from his office. Advise in the given situation, the tenability of maintenance of complaint against Mr. Zubin.

ANSWERS

Answer to Multiple Choice Questions

1.	c	2.	b	3.	d	4.	c	5.	c

Answer to Descriptive Answers

1. **Removal of Member of the SEBI (Section 6 of the Securities and Exchange Board of India Act, 1992)**

According to section 6 of the Securities and Exchange Board of India Act, 1992, the Central Government shall have the power to remove a member appointed to the Board, if he/she :

- (i) is, or at any time has been adjudicated as insolvent;
- (ii) is of unsound mind and stands so declared by a competent court;
- (iii) has been convicted of an offence which, in the opinion of the Central Government, involves a moral turpitude.

- (iv) has, in the opinion of the Central Government so abused his position as to render his continuance in office detrimental to the public interest.

Before removing a member, he will be given a reasonable opportunity of being heard in the matter.

In the present case, a group of complainants have alleged that Mr. Z, a member of the SEBI has pecuniary interest in some of the cases that came up before the Board and he misused his position and therefore, he should be removed from his office.

Here, above complainants may approach the Central Government for removal of Mr. Z, a member of the SEBI and if the Central Government is of the opinion that Mr. Z has so abused his position as to render his continuation in office detrimental to the public interest, the Central Government may remove Mr. Z from his office after giving him a reasonable opportunity of being heard in the matter.

2. Price manipulation in the shares of ABC Ltd. can be considered as fraudulent and unfair trade practices relating to securities market. In this case SEBI may exercise the following powers under section 11(4) of securities and Exchange Board of India Act, 1992.

- (i) Suspend the trading of any security (in this case the securities of ABC Ltd.) in a recognized stock exchange.
- (ii) Restrain persons (in this case ABC Ltd.) from accessing the securities market. It can also prohibit any person associated with securities market (i.e. brokers who have indulged in price manipulation) to buy, sell or deal in securities market.

SEBI may issue the above orders for reasons to be recorded in writing. SEBI shall, either before or after passing such orders give an opportunity of hearing to company and brokers concerned (proviso 2 to Section 11(4)) SEBI may also appoint an adjudicating officer who may levy penalty under section 15 HA after holding an enquiry in the prescribed manner. According to section 15HA if any person indulges in fraudulent and unfair trade practices relating to securities, he shall be liable to a penalty which shall not be less than five lakh rupees but which may extend to twenty-five crore rupees or three times the amount of profits made out of such practices, whichever is higher.

Prohibition on manipulation and deceptive practices: Further according to section 12A, no person shall directly or indirectly indulge in following (i.e.) (a) using in manipulative or deceptive device in connection with purchase, sale or securities listed (b) Employ any scheme or device to defraud in connection with dealing in securities which are listed (c) engage in an act which would operate as fraud or deceit upon any person in connection with dealing in securities which are listed. SEBI may impose penalty which shall not be less than one lakh rupees but which may extend to one crore rupees. (Section 15 HB).

3. **Remedies against SEBI order:** Section 15B of the Securities and Exchange Board of India Act, 1992 lays down that if any person, who is registered as an intermediary and is required

under this Act or any rules or regulations made there under, to enter into an agreement with his client, fails to enter into such agreement, he shall be liable to a penalty of one lakh rupees for each day during which such failure continues or one crore rupees, whichever is less. Mr. Clever has been penalised under the above mentioned provision. Two remedies are available to Mr. Clever in this matter:-

- (i) **Appeal to the Securities Appellate Tribunal:** Section 15T of the SEBI Act, (1) any person aggrieved,—
 - (a) by an order of the Board made, on and after the commencement of the Securities Laws (Second Amendment) Act, 1999, under this Act, or the rules or regulations made there under; or
 - (b) by an order made by an adjudicating officer under this Act; or
 - (c) by an order of the Insurance Regulatory and Development Authority or the Pension Fund Regulatory and Development Authority, may prefer an appeal to a Securities Appellate Tribunal having jurisdiction in the matter.

Every appeal shall be filed within a period of forty-five days from the date on which a copy of the order made by the Board or the Adjudicating Officer or the Insurance Regulatory and Development Authority or the Pension Fund Regulatory and Development Authority, as the case may be, is received by him and it shall be in such form and be accompanied by such fee as may be prescribed:

Provided that the Securities Appellate Tribunal may entertain an appeal after the expiry of the said period of forty-five days if it is satisfied that there was sufficient cause for not filing it within that period.

On receipt of an appeal under sub-section (1), the Securities Appellate Tribunal may, after giving the parties to the appeal, an opportunity of being heard, pass such orders thereon as it thinks fit, confirming, modifying or setting aside the order appealed against.

The Securities Appellate Tribunal shall send a copy of every order made by it to the Board, or the Insurance Regulatory and Development Authority or the Pension Fund Regulatory and Development Authority, as the case may be the parties to the appeal and to the concerned Adjudicating Officer.

The appeal filed before the Securities Appellate Tribunal under sub-section (1) shall be dealt with by it as expeditiously as possible and endeavor shall be made by it to dispose of the appeal finally within six months from the date of receipt of the appeal.

- (ii) **Appeal to the Supreme Court:** Section 15Z of the SEBI Act, 1992 provides that any person aggrieved by any decision or order of the Securities Appellate Tribunal may file an appeal to the Supreme Court within 60 days from the date of communication of

the decision or order to him on any question of fact or law arising out of such order. The Supreme Court may, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within the said period, allow it to be filed within a further period not exceeding 60 days.

4. **The Securities and Exchange Board of India (SEBI) was established primarily for the purpose of**

1. to protect the interests of investors in securities
2. to promote the development of securities market
3. to regulate the securities market and
4. For matters connected therewith and incidental thereto.

The following defaults by stock brokers come within the purview of SEBI Act:

- (a) Any failure on the part of the stock broker to issue contract notes in the form and in the manner specified by the Stock Exchange.
- (b) Any failure on the part of the broker to deliver any security or to make payment of the amount due to the investor in the manner or within the period specified in the regulations.
- (c) Any collection of charges by way of brokerage in excess of the brokerage as specified in the regulations. (Section 15 F, SEBI Act, 1992)

5. Securities and Exchange Board of India (SEBI) was established for regulating the various aspects of stock market. One of its functions is to register and regulate the stock brokers. In the light of this, Mr. Raman is advised that the complaint against the erring stock broker may be submitted to SEBI.

The grounds on which or the defaults for which complaints may be made to SEBI are as follows:

- (a) Any failure on the part of the stock broker to issue contract notes in the form and manner specified by the stock exchange of which the stock broker is a member.
- (b) Any failure to deliver any security or any failure to make payment of the amount due to the investor in the manner within the period specified in the regulations.
- (c) Any collection of charges by way of brokerage which is in excess of the brokerage specified in the regulations.

6. Section 15G of the Securities and Exchange Board of India (SEBI) Act, 1992 deals with penalty for Insider Trading. According to this, if any insider

- (i) either on his own behalf or on behalf of any other person, deals in securities of a body corporate on any stock exchange on the basis of any unpublished price sensitive information; or
- (ii) communicates any unpublished price sensitive information to any person, with or without his request for such information except as required in the ordinary course of business or under any law, or
- (iii) counsels or procures for, any other person to deal in any securities of any body corporate on the basis of unpublished price sensitive information,

shall be liable to a penalty of twenty-five crore rupees or three times the amount of profits made out of insider trading, whichever is higher. As such SEBI can, after following the prescribed procedure, impose a penalty on Mr. P. Mehta. The maximum penalty that SEBI can impose is Rupees twenty-five crores or three times the amount of profits made out of insider trading, whichever is higher.

7. As per section 11 (4) of the Securities and Exchange Board of India Act, 1992, the Board may, by an order, for reasons to be recorded in writing, in the interest of investors or securities market, take any of the following measures, either pending investigation or inquiry or on completion of such investigation or inquiry, namely:—

- 1. suspend the trading of any security in a recognised stock exchange;
- 2. restrain persons from accessing the securities market and prohibit any person associated with securities market to buy, sell or deal in securities;
- 3. suspend any office-bearer of any stock exchange or self-regulatory organization from holding such position;
- 4. impound and retain the proceeds or securities in respect of any transaction which is under investigation;
- 5. attach, for a period not exceeding ninety days, bank accounts or other property of any intermediary or any person associated with the securities market in any manner involved in violation of any of the provisions of this Act, or the rules or the regulations made thereunder:

Provided that the Board shall, within ninety days of the said attachment, obtain confirmation of the said attachment from the Special Court, established under section 26A, having jurisdiction and on such confirmation, such attachment shall continue during the pendency of the aforesaid proceedings and on conclusion of the said proceedings, the provisions of section 28A shall apply:

Provided further that only property, bank account or accounts or any transaction entered therein, so far as it relates to the proceeds actually involved in violation of any of the provisions of this Act, or the rules or the regulations made thereunder shall be

allowed to be attached.

6. direct any intermediary or any person associated with the securities market in any manner not to dispose of or alienate an asset forming part of any transaction which is under investigation.

The amount disgorged, pursuant to a direction issued, under the SEBI Act or the Securities Contracts (Regulation) Act, 1956 or the Depositories Act, 1996, as the case may be-

- shall be credited to the Investor Protection and Education Fund (IPEF) established by the Board, and
- such amount shall be utilised by the Board in accordance with the regulations made under this Act.”.

Provided that the Board may take any of the measures specified in clause (d) or clause (e) or clause (f), in respect of any listed public company or a public company (not being intermediaries referred to in section 12) which intends to get its securities listed on any recognised stock exchange where the Board has reasonable grounds to believe that such company has been indulging in insider trading or fraudulent and unfair trade practices relating to securities market :

Provided further that the Board shall, either before or after passing such orders, give an opportunity of hearing to such intermediaries or persons concerned.

Penalty: The Board may, by an order, for reasons to be recorded in writing, levy penalty under sections 15A, 15B, 15C, 15D, 15E, 15EA, 15EB, 15F, 15G, 15H, 15HA and 15HB after holding an inquiry in the prescribed manner.

8. According to Section 28A of the Securities and Exchange Board of India Act, 1992, if a person fails to pay the penalty imposed by the adjudicating officer or fails to comply with any direction of the Board for refund of monies or fails to comply with a direction of disgorgement order issued under section 11B or fails to pay any fees due to the Board, the Recovery Officer may draw up under his signature a statement /certificate in the specified form specifying the amount due from the person and shall proceed to recover from such person the amount specified in the certificate by one or more of the following modes, namely:
 - (a) attachment and sale of the person's movable property;
 - (b) attachment of the person's bank accounts;
 - (c) attachment and sale of the person's immovable property;
 - (d) arrest of the person and his detention in prison;
 - (e) appointing a receiver for the management of the person's movable and immovable properties.

The expression 'Recovery Officer' means any officer of the Board who may be authorized by general or special order in writing, to exercise the powers of a Recovery Officer. The Recovery Officer shall be empowered to seek the assistance of the local district administration while exercising the powers.

9. **Audit Committee:** According to Regulation 18 of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, every listed entity shall constitute a qualified and independent audit committee which shall have:

- (a) Minimum three directors as members.
- (b) At least Two-thirds of the members of audit committee shall be independent directors.
- (c) All members of audit committee shall be financially literate and at least one member shall have accounting or related financial management expertise.

As per the facts of the question, M/s MKBTC Limited, listed its securities in a recognised stock exchange in the month of August, 2019. In order to comply with the requirements of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, the company requires to do the following:

- (i) The audit committee of M/s MKBTC Limited already has 7 directors as members, which is in compliance.
- (ii) The audit committee has 4 directors as independent directors. However, once the company gets listed, at least 5 $[7 \times (2/3)]$ directors shall be independent directors. Thus, they need to change the composition of audit committee once the company gets listed on stock exchange.
- (iii) In the existing audit committee though majority of the members have the ability to read and understand the financial statement but none of them has accounting or related financial management expertise. However, once the company gets listed it is required that all members of audit committee shall be financially literate and at least one member shall have accounting or related financial management expertise. Hence, it is required that the company should appoint at least one member in the audit committee who shall have accounting or related financial management expertise.

In view of above, the existing audit committee cannot continue after listing of its securities.

10. According to section 6 of the Securities and Exchange Board of India Act, 1992, the Central Government shall have the power to remove a member appointed to the Board, if he/she:
- (i) is, or at any time has been adjudicated as insolvent;
 - (ii) is of unsound mind and stands so declared by a competent court;
 - (iii) has been convicted of an offence which, in the opinion of the Central Government, involves a moral turpitude.

- (iv) has, in the opinion of the Central Government so abused his position as to render his continuance in office detrimental to the public interest.

Before removing a member, he will be given a reasonable opportunity of being heard in the matter.

In the present case, a group of complainants have alleged that Mr. Zubin, a member of the SEBI is being adjudicated as an insolvent. His state of position may effect on rendering of his services in a biased manner. This may be unfavorable to the public interest and so should be removed from his office.

Here, above complainants may approach the Central Government for removal of Mr. Zubin, and if the Central Government is of the opinion that Mr. Zubin was not competent in rendering of his services/duties in a office as a member of the Board. The Central Government may remove Mr. Zubin from his office in compliance with the said provision.

[illegible]

CHAPTER

1

THE FOREIGN EXCHANGE MANAGEMENT ACT, 1999



LEARNING OUTCOMES

After reading this chapter, you will be able to:

- ❑ Explain important terms and definition under the Foreign Exchange Management Act, 1999
- ❑ Determine and explain the concept of Residential Status under the Foreign Exchange Management Act, 1999
- ❑ Identify and explain nature of Current and Capital Account Transactions and the Rules and Regulations governing them
- ❑ The role of Authorised Persons under the Foreign Exchange Management Act, 1999
- ❑ Regulations governing the transactions in relations to import and export of goods and services, and Rules and Regulation governing Overseas Investments (OI)
- ❑ Comprehend Process of loans made by non-resident lenders in foreign currency to Indian borrowers
- ❑ Mention the penalties imposed under the Act and the process of adjudication and the Appellate procedure under the Act.



1. INTRODUCTION

Need for the Act

The change in the economic scenario, globalization of capital, free trade across the globe, necessitated the need for managing foreign exchange in the country in an orderly manner. To facilitate cross border trade and cross border capital flows, exchange control law was required. Foreign exchange control led to introduction of exchange control law through Defense of India rules by the Britishers in 1939. Subsequently, Foreign Exchange Regulation Act (FERA) was enacted in 1947 which was later replaced with 'the Foreign Exchange Regulation Act, 1973' (FERA).



Government as part of its agenda of liberalisation of the Indian economy in 1991, permitted free movement of foreign exchange in connection trade related receipts and payments as well as Foreign Investment in various sectors. This increased the flow of foreign exchange to India and consequently foreign exchange reserves increased substantially. The Foreign Exchange Management Act, 1999 has been made effective from 1st June, 2000. This Act enables management of foreign exchange reserves for the country.

Salient Features of the Act: It provides for-

- Regulation of transactions between residents and non-residents
- Investments in India by non-residents and overseas investments by Indian residents
- Freely permissible transactions on current account subject to reasonable restrictions that may be imposed
- RBI and Central Government control over capital account transactions
- Requirement for realisation of export proceeds and repatriation to India
- Dealing in foreign exchange through 'Authorised Persons' like Authorised Dealer/Money Changer/Off-shore banking unit
- Adjudication and Compounding of Offences
- Investigation of offences by Directorate of Enforcement
- Appeal provisions including Special Director (Appeals) and Appellate Tribunal.

Enforcement of FEMA: Though RBI exercises overall control over foreign exchange transactions, enforcement of FEMA has been entrusted to a separate 'Directorate of Enforcement' formed for this purpose. [Section 36].

Broad Structure of FEMA

Now let us have a glance at the broad structure the Act. The Act consists of 7 Chapters dealing with following areas:

Chapters	Matters	Sections
I	Preliminary	1 – 2
II	Regulation and Management of Foreign Exchange	3 – 9
III	Authorised Person	10 – 12
IV	Contravention and Penalties	13 – 15
V	Adjudication and Appeal	16 – 35
VI	Directorate of Enforcement	36 – 38
VII	Miscellaneous	39 – 49

2. PREAMBLE, EXTENT, APPLICATION AND COMMENCEMENT OF FEMA, 1999

(A) Preamble: This Act aims to consolidate and amend the law relating to foreign exchange with the objective of —

- (i) facilitating external trade and payments and
- (ii) for promoting the orderly development and maintenance of foreign exchange market in India.

(B) Extent and Application [Sections 1]: FEMA, 1999 extends to the whole of India. In addition, it shall also apply to all branches, offices and agencies outside India owned or controlled by a person resident in India and also to any contravention thereunder committed outside India by any person to whom this Act applies.

The scope of the Act has been extended to include branches, offices and agencies outside India. The scope is thus wide enough because the emphasis is on the words “Owned or Controlled”. Contravention of the FEMA committed outside India by a person to whom this Act applies will also be covered by FEMA.

(C) Commencement: The Act, 1999 came into force with effect from 1st June, 2000 vide Notification G.S.R. 371(E), dated 1.5.2000.



3. DEFINITIONS [SECTION 2]

In this Act, unless the context otherwise requires:

- (a) **“Adjudicating Authority”** means an officer authorised under sub-section (1) of section 16(1); [Section 2(a)]
- (b) **“Appellate Tribunal”** means the Appellate Tribunal for Foreign Exchange established under section 18; [Section 2(b)]
- (c) **“Authorised person”** means an authorised dealer, money changer, off-shore banking unit or any other person for the time being authorised under section 10(1) to deal in foreign exchange or foreign securities; [Section 2(c)]
- (d) **“Capital Account Transaction”** means a transaction, which alters the assets or liabilities, including contingent liabilities, outside India of persons resident in India or assets or liability in India of persons resident outside India, and includes transactions referred to in ¹Section 6(3); [Section 2(e)]
- (e) **“Currency”** includes all currency notes, postal notes, postal orders, money orders, cheques, drafts, travelers’ cheques, letters of credit, bills of exchange and promissory notes, credit cards or such other similar instruments, as may be notified by the Reserve Bank. [Section 2(h)]
- (f) **“Currency Notes”** means and includes cash in the form of coins and bank notes; [Section 2(i)]
- (g) **“Current Account Transaction”** means a transaction other than a capital account transaction and without prejudice to the generality of the foregoing such transaction includes,
 - (i) payments due in connection with foreign trade, other current business, services, and short-term banking and credit facilities in the ordinary course of business.
 - (ii) payments due as interest on loans and as net income from investments.
 - (iii) remittances for living expenses of parents, spouse and children residing abroad, and
 - (iv) expenses in connection with foreign travel, education and medical care of parents, spouse and children; [Section 2(j)]
- (h) **“Export”**, with its grammatical variations and cognate expressions means;
 - (i) the taking out of India to a place outside India any goods.
 - (ii) provision of services from India to any person outside India; [Section 2(l)]
- (i) **“Foreign Currency”** means any currency other than Indian currency; [Section 2(m)]
- (j) **“Foreign Exchange”** means foreign currency and includes:

¹ Section 6(3) has been deleted with effect from 15th October 2019.

- (i) deposits, credits and balances payable in any foreign currency,
- (ii) drafts, travelers' cheques, letters of credit or bills of exchange, expressed or drawn in Indian currency but payable in any foreign currency,
- (iii) drafts, travelers' cheques, letters of credit or bills of exchange drawn by banks, institutions or persons outside India, but payable in Indian currency; [Section 2(n)]
- (k) **"Foreign Security"** means any security, in the form of shares, stocks, bonds, debentures or any other instrument denominated or expressed in foreign currency and includes securities expressed in foreign currency, but where redemption or any form of return such as interest or dividends is payable in Indian currency; [Section 2(o)]
- (l) **"Import"**, with its grammatical variations and cognate expressions, means bringing into India any goods or services; [Section 2(p)]
- (m) **"Person"** includes:
 - (i) an individual,
 - (ii) a Hindu undivided family,
 - (iii) a company,
 - (iv) a firm,
 - (v) an association of persons or a body of individuals, whether incorporated or not,
 - (vi) every artificial juridical person, not falling within any of the preceding sub-clauses, and;
 - (vii) any agency, office or branch owned or controlled by such person; [Section 2(u)]
- (n) **"Person resident in India"** means:
 - (i) a person residing in India for more than 182 days during the course of the preceding financial year but does not include—
 - (A) a person who has gone out of India or who stays outside India, in either case—
 - (a) for or on taking up employment outside India, or
 - (b) for carrying on outside India a business or vocation outside India, or
 - (c) for any other purpose, in such circumstances as would indicate his intention to stay outside India for an uncertain period;
 - (B) a person who has come to or stays in India, in either case, otherwise than:
 - (a) for or on taking up employment in India, or
 - (b) for carrying on in India a business or vocation in India, or

- (c) for any other purpose, in such circumstances as would indicate his intention to stay in India for an uncertain period;
- (ii) any person or body corporate registered or incorporated in India,
- (iii) an office, branch or agency in India owned or controlled by a person resident outside India,
- (iv) an office, branch or agency outside India owned or controlled by a person resident in India; [Section 2(v)]
- (o) **“Person Resident Outside India”** means a person who is not resident in India; [Section 2(w)]
- (p) **“Repatriate to India”** means bringing into India the realised foreign exchange and
 - (i) the selling of such foreign exchange to an authorised person in India in exchange for rupees, or
 - (ii) the holding of realised amount in an account with an authorised person in India to the extent notified by the Reserve Bank.

It includes use of the realised amount for discharge of a debt or liability denominated in foreign exchange and the expression “repatriation” shall be construed accordingly; [Section 2(y)]

- (q) **“Security”** means shares, stocks, bonds and debentures, Government securities as defined in the Public Debt Act, 1944, savings certificates to which the Government Saving Certificates Act, 1959 applies, deposit receipts in respect of deposit of securities and units of the Unit Trust of India established under sub-section (1) of section 3 of the Unit Trust of India Act, 1963 or of any mutual fund and includes certificates of title to securities, but does not include bills of exchange or promissory notes other than Government promissory notes or any other instruments which may be notified by the Reserve Bank as security for the purposes of this Act; [Section 2(za)]
- (r) **“Service”** means service of any description which is made available to potential users and includes the provision of facilities in connection with banking, financing, insurance, medical assistance, legal assistance, chit fund, real estate, transport, processing, supply of electrical or other energy, boarding or lodging or both, entertainment, amusement or the purveying of news or other information, but does not include the rendering of any service free of charge or under a contract of personal service; [Section 2(zb)]
- (s) **“Transfer”** includes sale, purchase, exchange, mortgage, pledge, gift, loan or any other form of transfer of right, title, possession or lien. [Section 2(ze)]



4. RESIDENTIAL STATUS UNDER FEMA, 1999

The definition of “person” is similar to the definition contained in the Income-tax Act, 1961. The term ‘person’ includes entities such as companies, firms, individuals, HUF, Association of Persons (AOP), artificial juridical persons agencies, as well as offices and branches. Agencies, offices and branches do not have independent status separate from their owners. Yet these have been considered as persons. Under FEMA such offices and branches are included in definition of Person Resident in India. Therefore, they have been included in the definition of “Person”.

The term ‘person resident in India’ means the following entities:

1. A person who resides in India for more than 182 days during the preceding financial year;

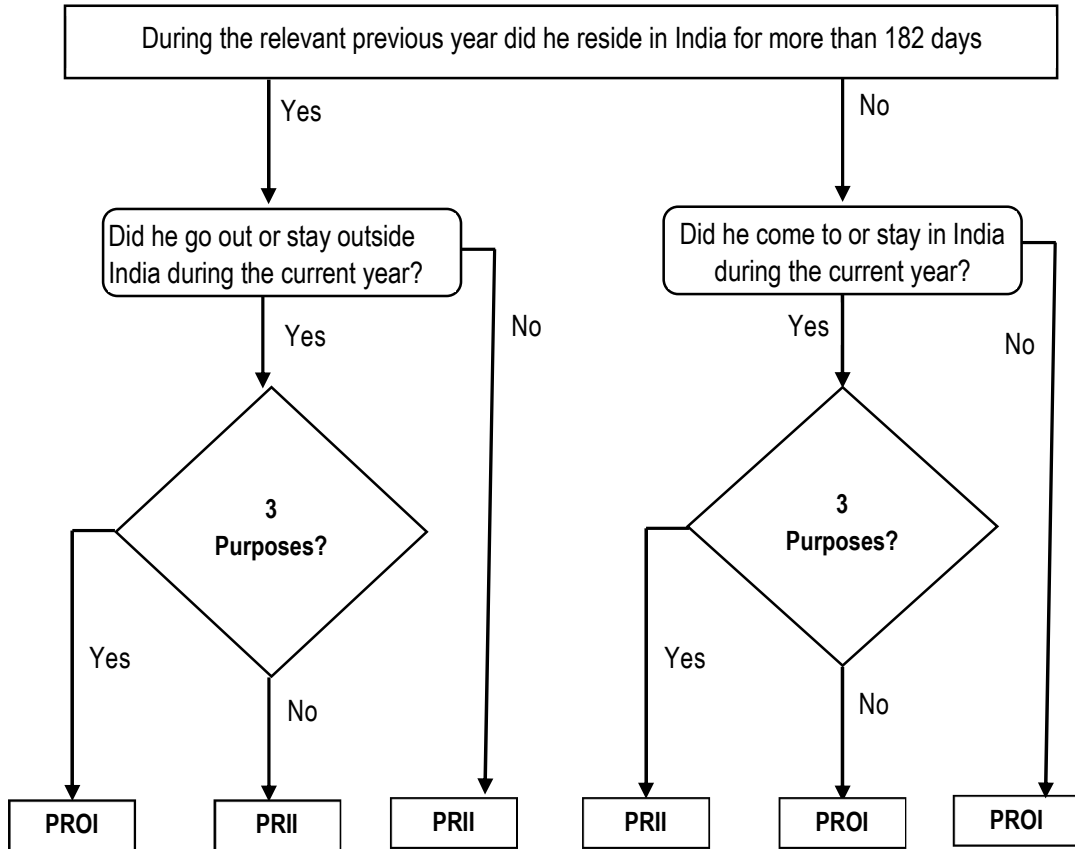
The following persons are NOT persons resident, in India even though they may have resided in India for more than 182 days.

- A. A person who has gone out of India or stays outside India for any of the three purposes given below,
- B. A person who has come to or stays in India OTHERWISE THAN for any of the three purposes given below;

Three Purposes

- (i) For or on taking up Employment
 - (ii) For carrying on a business or Vacation
 - (iii) For any other purpose in such circumstances as would indicate stay for an uncertain period.
- 2. Any person or body corporate registered or incorporated in India;
 - 3. An office, branch or agency in India owned or controlled by a person resident outside India;
 - 4. An office, branch or agency outside India owned or controlled by a person resident in India.

Person resident outside India means a person who is **not** resident in India.



As the definitions of Person Resident in India (PRII) and Person Resident outside India (PROI) are quite relevant for determining the applicability of the Act on an entity, let us analyse and understand it better.

In the case of individuals, to be considered as “resident”, the person should have resided in India in the preceding financial year for more than 182 days. **Citizenship is not the criteria for determining whether or not a person is resident in India.**

There are three limbs in the definition. The first limb prescribes the number of days stay. Then there are two limbs which are exceptions to the first limb.

First limb – It states that a person who is in India for more than 182 days in the “preceding year” will be a Person Resident in India. Thus, at the threshold or basic level, one has to consider the period of stay during the preceding year.

Example 1: If a person resides in India for more than 182 days during FY 2018-19, then for the FY 2019-20, the person will be an Indian resident. For FY 2018-19, one will have to consider residence during FY 2017-18, and so on.

There are two exceptions provided in clauses (A) and (B). Clause (A) is for persons going out of India. Clause (B) is for persons coming into India. Exceptions carve out situations that do not fall under the main body of a section, even though they satisfy the criteria. This means that even if a person is an Indian resident based on the test provided in the first limb, the person will be a "Person Resident Outside India (PROI) if he falls within limb (A) or limb (B).

Clause (A) – second limb – It states that if a person leaves India in any of the THREE PURPOSES we saw above, he will not be a PRII. He will be a PROI.

Thus, in the **example** given for the first limb above, if a person leaves India on 1st November 2019, he will be a non-resident from 2nd November 2019 – even though his number of days in India was more than 182 days in FY 2018-19. Similarly, if a person goes and stays out of India for carrying on any business, he will be a PROI from that date. For FY 2019-20 the person will be a PRII till 1st November 2019. He will then be a PROI. From 1st April 2020, the person will continue to be a PROI as long as he stays out of India for employment.

An **example** for clause (iii) can be a person who has a green card in the USA. The green card entitles a person to stay in the USA and eventually become a US citizen. If a person goes abroad and starts staying in the USA, he will be a non-resident from that date as his stay abroad indicates that he is going to stay there for an uncertain period.

Clause (B) – third limb – This is a complex clause as first limb read with third limb has two exceptions. Limb one uses the phrase "but does not include". Third limb uses the phrase "otherwise than". Use of two exceptions make it complex reading.

It states that if a person has come to India **for any reason otherwise than** for - employment, business or circumstances which indicate his intention to stay for uncertain period – he will be a non-resident. This will be so even if the person has stayed in India for more than 182 days in the preceding year.

For **example**, if a person comes to India on 1st June 2019 for visiting his parents. However, his parents fall sick and he stays till 31st March 2020. Thereafter he continues to stay in India. It is however certain that he will leave India in next 6 months when his parents recover. His stay in India is neither for employment, nor for business, nor for circumstances which show that he will stay in India for an uncertain period. In such a case, even if he has resided in India for more than 182 days in FY 2019-20, he will continue to be a non-resident from 1st April 2020 also. In FY 2019-20, he is of course a PROI as he did not reside in India for more than 182 in FY 2018-19.

If a person comes to India on 1st June 2019 for employment, business or circumstances which indicate his intention to stay in India for an uncertain period, he will be a PRII from 1st June 2019.

Residential status is not for a year. It is from a particular date. This is different from income-tax law. Under income-tax law, a person has to pay tax in respect of the income of the previous year. Therefore, it is possible to look at a complete year for determining residential status under the Income Tax Act, 1961. FEMA is a regulatory law. One has to know the person's status at the time of undertaking a

transaction. If for **example**, a person comes to India for employment, and if his status can be known only when the year is completed, how will he and other people enter into commercial transactions with each other? If he is considered as a PROI till the year is over, then people will not be able to enter into transactions with him. This is the reason why the residential status is not for a year but from particular date.

It is understood that this condition applies only to individuals. It will not apply to HUF, AOP or artificial juridical person as they cannot get employed, cannot go out of India or come to India. Hence, they do not come within the ambit of the second and third limbs. These entities like HUF and AOP are not required to be registered or incorporated like corporate entities nor the definition can be far stretched to cover by applying the criteria of 'owned or controlled'. Hence legally the definition for HUF, AOP, BOI fail. Practically if the HUF, AOP etc. are in India, they will be considered as Indian residents.

Person or Body corporate: Any person or body corporate registered or incorporated in India, will be considered a PRII. This definition too, does not apply to AOP, BOI etc.

Office, branch or agency: Any agency, branch or agency outside India but **owned or controlled by PRII** will be considered as person resident in India (PRII). Thus, one cannot set up a branch outside India and attempt to avoid FEMA provisions.

Any agency, branch or agency in India but **owned or controlled by a person resident outside India (PROI)** will be considered as a person resident in India. This is relevant as Indian residents can deal with such branch in India without considering FEMA. If such branch is considered as a PROI then it will be difficult to undertake several transactions.

Illustration: Mr. X had resided in India during the financial year 2019-2020 for less than 182 days. He had come to India on April 1, 2020 for carrying on business. He intends to leave the business on April 30, 2021 and leave India on June 30, 2021. Determine his residential status for the financial years 2020-2021 and 2021-2022 up to the date of his departure?

Answer: As explained in the above example, Mr. X will be considered as a person resident in India' from 1st April 2020. As regards, financial year 2021-2022, Mr. X would continue to be an Indian resident from 1st April 2021.

If he leaves India for the purpose of taking up employment or for business/vocation outside India, or for any other purpose as would indicate his intention to stay outside India for an uncertain period, he would cease to be person resident in India from the date of his departure. It may be noted that even if Mr. X is a foreign citizen, if he has not left India for any these purposes, he would be considered, 'person resident in India' during the financial year 2021-2022. Thus, it is the purpose of leaving India which will decide his status from 1st July 2021.

Illustration: Mr. Z had resided in India during the financial year 2019-2020. He left India on 1st August, 2020 for United States for pursuing higher studies for three years. What would be his residential status during financial year 2020-2021 and during 2021-2022?

Answer: Mr. Z had resided in India during financial year 2019-2020 for more than 182 days. After that he has gone to USA for higher studies. He has not gone out of or stayed outside India for or on taking up employment, or for carrying a business or for any other purpose, in circumstances as would indicate his intention to stay outside India for an uncertain period. Accordingly, he would be 'person resident in India' during the financial year 2020-2021. RBI has however clarified in its AP circular no. 45 dated 8th December 2003, that students will be considered as non-residents. This is because usually students start working there to take care of their stay and cost of studies.

For the financial year 2021-2022, he would not have been in India in the preceding financial year (2020-2021) for a period exceeding 182 days. Accordingly, he would not be 'person resident in India' during the financial year 2021-2022.

Illustration: Toy Ltd. is a Japanese company having several business units all over the world. It has a robotic unit with its head quarters in Mumbai and has a branch in Singapore. The Headquarters at Mumbai controls the Singapore branch of the robotic unit. What would be the residential status of the robotic unit in Mumbai and that of the Singapore branch?

Answer: Toy Ltd. being a Japanese company would be a person resident outside India. [Section 2(w)]. Section 2(u) defines 'person'. Under clause (viii) thereof person would include any agency, office or branch owned or controlled by such 'person'. The term such 'person' appears to refer to a person who is included in clauses (i) to (vi). Accordingly, robotic unit in Mumbai, being a branch of a company, would be a 'person'.

Section 2(v) defines 'person resident in India'. Under clause (iii) thereof 'person resident in India' would include an office, branch or agency in India owned or controlled by a person resident outside India. Robotic unit in Mumbai is owned or controlled by a person 'resident outside India'. Hence, it would be 'person resident in India'.

The robotic unit headquartered in Mumbai, which is a person resident in India as discussed above, controls the Singapore branch, Hence, the Singapore branch is a 'person resident in India'.

Illustration: Miss Alia is an airhostess with the British Airways. She flies for 12 days in a month and thereafter takes a break for 18 days. During the break, she is accommodated in 'base', which is normally the city where the Airline is headquartered. However, for security considerations, she was based at Mumbai. During the financial year, she was accommodated at Mumbai for more than 182 days. What would be her residential status under FEMA?

Answer: Miss Alia stayed in India at Mumbai 'base' for more than 182 days in the preceding financial year. She is however employed in UK. She has not come to India for employment, business or circumstances which indicate her intention to stay for uncertain period. Under section 2(v)(B), such persons are not considered as Indian residents even if their stay exceeds 182 days in the preceding year. Thus, while Miss Alia may have stayed in India for more than 182 days, she cannot be considered to be a Person Resident in India.

If however she has been employed in Mumbai branch of British Airways, then she will be considered a Person Resident in India.

Case law

Basant Kumar Sharma v. Government of India, Delhi High Court held that if NRI returns to stay in India for an 'uncertain period' he will become a person resident in India and his NRE account should be re-designated as Resident's account

In *K. Ramullan v. Commissioner of Income-tax*, it was held that for being a resident of India within FEMA, the stay has to be of some permanence and not with intention of returning abroad in some short, set period and it has to be a stay for taking up employment or carrying on business or a vocation with intention of remaining in India for an uncertain period.

In this case, person, though of Indian origin, had settled in Malaysia and also acquired Malaysian citizenship. His wife and children were residing in India. He stayed in India with his wife for undergoing medical treatment for 3 years. In this case, the person could not be treated as a person resident in India.



5. REGULATION AND MANAGEMENT OF FOREIGN EXCHANGE

❖ Dealing in foreign exchange, etc. [Section 3]

No person shall-

- (a) deal in or transfer any foreign exchange or foreign security to any person not being an authorised person (AP);
- (b) make any payment to or for the credit of any person resident outside India in any manner;
- (c) receive otherwise than through an authorised person, any payment by order or on behalf of any person resident outside India in any manner.

Explanation—For the purpose of this clause, where any person in, or resident in, India receives any payment by order or on behalf of any person resident outside India through any other person (including an authorised person) without a corresponding inward remittance from any place outside India, then, such person shall be deemed to have received such payment otherwise than through an authorised person;

- (d) enter into any financial transaction in India as consideration for or in association with acquisition or creation or transfer of a right to acquire, any asset outside India by any person.

The above transactions may carried on

- a. as otherwise provided in this Act; or
- b. with the general or special permission of the Reserve Bank.

Explanation — For the purpose of this clause, “financial transaction” means making any payment to, or for the credit of any person, or receiving any payment for, by order or on behalf of any person, or drawing, issuing or negotiating any bill of exchange or promissory note, or transferring any security or acknowledging any debt.

This section imposes blanket restrictions on the specified transactions. This section applies to PRIs and PROIs. The purpose of this section is to regulate inflow and outflow of Foreign Exchange through Authorised dealers and in a permitted manner.

Consider following examples:

- (i) **Example pertaining to clause (a)- Dealing in foreign exchange** – A PROI comes to India and would like to sell US\$ 1,000 to his friend who is resident in India. The friend offers him a rate better than the banks. This cannot be done as it would amount to dealing in foreign exchange.
- (ii) **Example pertaining to clause (b)** – A PROI has an insurance policy in India. He requests his brother in India to pay the insurance premium. This will amount to payment for the credit of non-resident. This is not permitted.
- (iii) **Example pertaining to clause (c)**– A foreign tourist comes to India and he takes food at a restaurant. He would like to pay US\$ 20 in cash to the restaurant. The restaurant cannot accept cash as it will be a receipt otherwise than through Authorised Person. The restaurant will have to take a money changers license to accept foreign currency.
- (iv) **Example pertaining to clause (d)**–Transactions covered by this sub-section are known as Hawala transactions. An Indian resident gives Rs` 70,000 in cash to an Indian dealer. For this transaction, the brother in Dubai will get US\$ 1,000 from a Dubai dealer. The two dealers may settle the transactions later. However, transaction is not permitted.

❖ **Holding of foreign exchange [Section 4]**

Except as provided in this Act, no person resident in India shall acquire, hold, own, possess or transfer any foreign exchange, foreign security or any immovable property situated outside India.

This section prevents Indian residents to acquire, hold, own, possess or transfer any foreign exchange, foreign security or immovable property abroad. Then through separate notifications, acquisition of these assets has been permitted subject to certain conditions and compliance rules.

Example 2: If an Indian resident receives bank balance of US\$ 10,000 from his uncle in London, the Indian resident cannot hold on to the foreign funds. He is supposed to bring back the funds as provided in section 8.

Case law

The Appellate Tribunal for Foreign Exchange Management Act, New Delhi gave the decision in *Dr. D. Rewatha Thera v. Joint Director, Directorate of Enforcement*, on holding of foreign exchange under FEMA read with the section 12 of the FCRA, 2020.

In the given case, a complaint was received from ex-managing trustee of a society, registered in India. A show cause notice was issued to society for contravening provisions of section 4 for holding foreign exchange outside India.

As per the facts, society had inherited said amount as per voluntary settlement deed executed by settlors being persons resident outside India. Since, the society was not registered under the Foreign Contribution (Regulation) Act, and was prohibited from accepting foreign contribution, it moved an application in office of Ministry of Home Affairs for obtaining prior permission of Central Government under the Foreign Contribution (Regulation) Act for acceptance of foreign contribution.

Since no permission was granted, society, decided to transfer said amount to its bank account maintained in Sri Lanka till Home Ministry grant permission. Society moved an application in office of Ministry of Home Affairs much prior to realisation of said amount for granting permission for repatriation of said amount. By transferring of funds in Sri Lanka and by making various application to Home Ministry for granting permission for repatriation of said amount, Society had taken all reasonable steps to realize and repatriate foreign currency in India.

Hence it was held that that Society could not be held guilty of violating provisions of section 4.

Current account transactions [Section 5]

The term 'Current Account Transaction' is defined negatively by Section 2(j) of the Act. It means a transaction **other than a capital account transaction** and includes the following types of transactions:

- (i) Payments in the course of ordinary course of foreign trade, other services such as short-term banking and credit facilities in the ordinary course of business etc.
- (ii) Payments in the form of interest on loans or income from investments.
- (iii) Remittances for living expenses of parents, spouse, or children living abroad
- (iv) Expenses in connection with foreign travel, education etc.

Example 3: An Indian resident imports machinery from a vendor in UK for installing in his factory. As per accounts and income-tax law, machinery is a "capital expenditure". However, under FEMA, it does not alter (create) an asset in India for the UK vendor. It does not create any liability to a UK vendor for the Indian importer. Once the payment is made, the Indian resident or the UK vendor neither owns nor is owed anything in the other country. Hence it is a Current Account Transaction.

Example 4: An Indian resident imports machinery from a vendor in UK for installing in his factory on a credit period of 3 months. As per accounts and income-tax law, for the credit period of 3 months, there

is a liability of the Indian importer to the UK vendor. Technically under FEMA also, it is a liability outside India. However, under definition of Current Account Transaction [S. 2(j)(i)], “short-term banking and credit facilities in the ordinary course of business” are considered as a Current Account Transaction. Hence import of machinery on credit terms is Current Account Transaction.

What if the credit period is 12 months? Under Master Directions for imports, payment has to be made within 6 months. If the credit period is in excess of 6 months, then the provisions of Trade Credit shall trigger. The provisions for Trade Credit are stated in Foreign Exchange Management (Borrowing and Lending) Regulations, 2018. For exports, the period for realisation of proceeds, is 9 months.

Example 5: A Person Resident in India transfers US\$ 1,000 to his NRI brother in New York as “gift”. The funds are sent from the PRII’s Indian bank account to the NRI brother’s bank account in New York. Under accounts and income-tax law, gift is a “capital receipt”. However, under FEMA, once the gift is accepted by the NRI, no one owns or owes anything to anyone in India or USA. The transaction is over. Hence it is a Current Account Transaction.

If gift is a current account transaction, why is there a restriction under Current Account regulations? It is because while there is no restriction on Current Account transactions, some reasonable restrictions can be imposed. Otherwise people may transfer funds abroad under the garb of current account transactions.

If however the PRII gives a PROI a gift in India in Indian currency, for the PROI it will result in funds lying in India (alteration of Indian asset). For PRII, there is no creation of asset or a liability. As this transaction creates an asset in India for the PROI, it is a Capital Account transaction. (Under separate rules, giving a gift in India to an NRI is permitted subject to certain rules.)

In a similar manner, if a PROI gives a gift to an PRII by remitting funds in India, there is no restriction. However, if the PROI gives the funds abroad, the resident cannot keep it abroad. He has to bring it to India.

Any person may sell or draw foreign exchange to or from an authorised person if such sale or drawal is a current account transaction.

The Central Government may, in public interest and in consultation with the Reserve Bank, impose such **reasonable restrictions** for current account transactions as prescribed under the FEM (Current Account Transactions) Rules, 2000.

The general rule to be understood is that Current Account transactions are freely permitted unless specifically prohibited and Capital Account transactions are prohibited unless specifically or generally permitted.

Section 5 of the Act permits any person to sell or draw Foreign Exchange to or from an Authorised person to undertake any current account transaction. The Central Government has the power to impose reasonable restrictions, in consultation with the RBI and in public interest on current account transactions. The Central Government has in exercise of this power issued the Foreign Exchange Management (Current Account Transactions) Rules, 2000.

Let us now see the various schedules to the Rules that lay down the restrictions:

I. SCHEDULE I

²Transactions for which drawal of foreign exchange is prohibited:

- (i) Remittance out of lottery winnings.
- (ii) Remittance of income from racing/riding, etc., or any other hobby.
- (iii) Remittance for purchase of lottery tickets, banned/prescribed magazines, football pools, sweepstakes etc.
- (iv) Payment of commission on exports made towards equity investment in Joint Ventures/Wholly Owned Subsidiaries abroad of Indian companies.
- (v) Remittance of dividend by any company to which the requirement of dividend balancing is applicable.
- (vi) Payment of commission on exports under Rupee State Credit Route, except commission up to 10% of invoice value of exports of tea and tobacco.
- (vii) Payment related to "Call Back Services" of telephones.
- (viii) Remittance of interest income on funds held in Non-resident Special Rupee Scheme a/c.

II. SCHEDULE II

³Transactions, which require prior approval of the Government of India for drawal of foreign exchange:

Purpose of Remittance	Ministry/Department of Govt. of India whose approval is required
Cultural Tours	Ministry of Human Resources Development (Department of Education and Culture)
Advertisement in foreign print media for the purposes other than promotion of tourism, foreign investments and international bidding (exceeding US\$ 10,000) by a State Government and its Public Sector Undertakings.	Ministry of Finance, Department of Economic Affairs
Remittance of freight of vessel chartered by a PSU	Ministry of Surface Transport (Chartering Wing)

²Schedule I (Transactions which are prohibited)-Foreign Exchange Management (Current Account Transactions) Rules, 2000 as amended from time to time.

³Schedule II (Transactions which require prior approval of the Central Government)- Foreign Exchange Management (Current Account Transactions) Rules, 2000 as amended from time to time

Payment of import through ocean transport by a Govt. Department or a PSU on c.i.f. basis (i.e., other than f.o.b. and f.a.s. basis)	Ministry of Surface Transport (Chartering Wing)
Multi-modal transport operators making remittance to their agents abroad	Registration Certificate from the Director General of Shipping
Remittance of hiring charges of transponders by (a) TV Channels (b) Internet service providers	Ministry of Information and Broadcasting Ministry of Communication and Information Technology.
Remittance of container detention charges exceeding the rate prescribed by Director General of Shipping	Ministry of Surface Transport (Director General of Shipping)
Remittance of prize money/sponsorship of sports activity abroad by a person other than International/National/State Level sports bodies, if the amount involved exceeds US \$ 100,000	Ministry of Human Resource Development (Department of Youth Affairs and Sports)
Remittance for membership of P & I Club	Ministry of Finance (Insurance Division)

Transactions which require RBI's prior approval for drawal of foreign exchange:

SCHEDULE III

1. Facilities for individuals—Individuals can avail of foreign exchange facility for the following purposes within the limit of USD 250,000 only.:

- (i) Private visits to any country (except Nepal and Bhutan)
- (ii) Gift or donation.
- (iii) Going abroad for employment
- (iv) Emigration
- (v) Maintenance of close relatives abroad
- (vi) Travel for business or attending a conference or specialised training or for meeting expenses for meeting medical expenses, or check-up abroad, or for accompanying as attendant to a patient going abroad for medical treatment/ check-up.
- (vii) Expenses in connection with medical treatment abroad
- (viii) Studies abroad
- (ix) Any other current account transaction

Any additional remittance in excess of the said limit for the said purposes shall require prior approval of the Reserve Bank of India.

However, for the purposes mentioned at item numbers (iv), (vii) and (viii) above, the individual may avail of exchange facility for an amount in excess of the limit prescribed under the Liberalised Remittance Scheme as provided in regulation 4 to FEMA Notification 1/2000-RB, dated the 3rd May, 2000 (here in after referred to as the said Liberalised Remittance Scheme) if it is so required by a country of emigration, medical institute offering treatment or the university, respectively:

Further, if an individual remits any amount under the said Liberalised Remittance Scheme in a financial year, then the applicable limit for such individual would be reduced from USD 250,000 (US Dollars Two Hundred and Fifty Thousand Only) by the amount so remitted:

Further, that for a person who is resident but not permanently resident in India and-

- (a) is a citizen of a foreign State **other than** Pakistan; or
- (b) is a citizen of India, who is on deputation to the office or branch of a foreign company or subsidiary or joint venture in India of such foreign company,

may make remittance up to his net salary (after deduction of taxes, contribution to provident fund and other deductions).

Explanation: For the purpose of this item, a person resident in India on account of his employment or deputation of a specified duration (irrespective of length thereof) or for a specific job or assignments, the duration of which does not exceed three years, is a resident but not permanently resident:

Further, a person other than an individual may also avail of foreign exchange facility, *mutatis mutandis*, within the limit prescribed under the said Liberalised Remittance Scheme for the purposes mentioned herein above.

2. Facilities for persons other than individual—The following remittances by persons other than individuals shall require prior approval of the Reserve Bank of India:

- (i) Donations exceeding one per cent. of their foreign exchange earnings during the previous three financial years or USD 5,000,000, whichever is less, for-
 - a. creation of Chairs in reputed educational institutes,
 - b. contribution to funds (not being an investment fund) promoted by educational institutes; and
 - c. contribution to a technical institution or body or association in the field of activity of the donor Company.
- (ii) Commission, per transaction, to agents abroad for sale of residential flats or commercial

plots in India exceeding USD 25,000 or five percent of the inward remittance whichever is more.

- (iii) Remittances exceeding USD 10,000,000 per project for any consultancy services in respect of infrastructure projects and USD 1,000,000 per project, for other consultancy services procured from outside India.

Explanation—For the purposes of this sub-paragraph, the expression “infrastructure” shall mean as defined in explanation to para 1(iv)(A)(a) of Schedule I of FEMA Notification 3/2000-RB, dated the May 3, 2000.

- (iv) Remittances exceeding five per cent of investment brought into India or USD 100,000 whichever is higher, by an entity in India by way of reimbursement of pre-incorporation expenses.

3. **Procedure**—The procedure for drawal or remittance of any foreign exchange under this schedule shall be the same as applicable for remitting any amount under the said Liberalised Remittance Scheme.

If the transaction is not listed in any of the above three schedules, it can be freely undertaken.

Exemption for remittance from RFC Account – No approval is required where any remittance has to be made for the transactions listed in Schedule II and Schedule III above from an RFC account.

Exemption for remittance from EEFC Account – If any remittance has to be made for the transactions listed in Schedule II and Schedule III above from EEFC account, then also no approval is required. However, if payment has to be made for the following transactions, approval is required even if payment is from EEFC account:

- Remittance for membership of P & I Club.
- Commission, per transaction, to agents abroad for sale of residential flats or commercial plots in India exceeding USD 25,000 or five per cent of the inward remittance whichever is more. Remittances exceeding five per cent of investment brought into India or USD 100,000 whichever is higher, by an entity in India by way of reimbursement of pre-incorporation expenses.

Exemption for payment by International Credit Card while on a visit abroad – If a person is on a visit abroad, he can incur expenditure stated in Schedule III if he incurs it through International credit card.

Note: Liberalised Remittance Scheme (LRS): Under the Liberalised Remittance Scheme (LRS), all resident individuals, including minors, are allowed to freely remit up to USD 250,000 per financial year (April – March) for any permissible current or capital account transaction or a combination of both. This

is inclusive of foreign exchange facility for the purposes mentioned in Para 1 of Schedule III of Foreign Exchange Management (CAT) Amendment Rules 2015, dated May 26, 2015.

In case of remitter being a minor, the LRS declaration form must be countersigned by the minor's natural guardian. The Scheme is not available to corporates, partnership firms, HUF, Trusts etc.

Consolidation of remittance of family members - Remittances under the Scheme can be consolidated in respect of family members subject to individual family members complying with its terms and conditions.

Exception: Clubbing is **not permitted** by other family members for **capital account transactions** such as opening a bank account/investment/purchase of property, if they are not the co-owners/co-partners of the overseas bank account/investment/property.

Case Law

In Board of Control for Cricket in India (BCCI) v. Special Director, Directorate of Enforcement, Mumbai, Appellate Tribunal for Foreign Exchange Management Act, New Delhi gave the decision as per section 42, read with section 5, of the Foreign Exchange Management Act, 1999 which dealt with the contravention by companies.

As per the facts, an agreement between Cricket South Africa (CSA) and BCCI, IPL-2 was organized in South Africa in April-May 2009 on payment of fixed fee by BCCI. The Competent authority, by impugned order imposed penalty upon appellants i.e., BCCI and its officers, for contravention of provisions of FEMA.

It was held that as there was no allegation in show cause notice that transactions, in question were Capital Account Transaction, it was difficult to conclude about nature of transaction particularly when appellants claimed that those were Current Account transactions for which no permission of RBI was necessary.

Since BCCI was not a company but only an Association, having been registered as a society, BCCI could not be treated as 'company' as per Explanation provided under section 42 of FEMA, 1999 and, therefore, appellant office bearers of BCCI could not be penalised under section 42.

IMPORT OF GOODS AND SERVICES: Import of Goods and Services into India is being allowed in terms of Section 5 of the Foreign Exchange Management Act 1999, read with Notification No. G.S.R. 381(E) dated May 3, 2000 viz. Foreign Exchange Management (Current Account Transaction) Rules, 2000. It is regulated by Master Direction – Import of Goods and Services updated from time to time.

As per the section I of the Master Direction – Import of Goods and Services, Import trade is regulated by the Directorate General of Foreign Trade (DGFT) under the Ministry of Commerce & Industry, Department of Commerce, Government of India. Authorised Dealer Category – I banks should ensure that the imports into India are in conformity with the Foreign Trade Policy in force and Foreign Exchange Management (Current Account Transactions) Rules, 2000 and the Directions issued by Reserve Bank under Foreign Exchange Management Act, 1999 from time to time.

General Guidelines for Imports: These General Guidelines deals with the imports relating to foreign exchange transactions.

(1) **General Guidelines:** Rules and regulations to be followed by the Authorised Dealer (AD) from the foreign exchange angle while undertaking import payment transactions on behalf of their clients are given in this para of the Section II of the Master direction. Where specific regulations do not exist, AD may be governed by normal trade practices and it may particularly adhere to "Know Your Customer" (KYC) guidelines (issued by Reserve Bank) in all their dealings.

(2) **Remittances for Import Payments:** AD may allow remittance for making payments for imports into India, after ensuring that all the requisite details are made available by the importer and the remittance is for bona fide trade transactions as per applicable laws in force.

(3) **Obligation of Purchaser of Foreign Exchange:** Following are the obligations to be complied with by the purchaser:

(i) **Utilization of acquired Foreign Exchange:** In terms of Section 10(6) of the Foreign Exchange Management Act, 1999 (FEMA), any person acquiring foreign exchange is permitted to use it either for the purpose mentioned in the declaration made by him to an Authorised Person or for any other purpose for which acquisition of foreign exchange is permissible under the said Act or Rules or Regulations framed there under.

(ii) **Evidence of import:** Where foreign exchange acquired has been utilised for import of goods into India, the AD should ensure that the importer furnishes evidence of import viz., as in IDPMS, Postal Appraisal Form or Customs Assessment Certificate, etc., and satisfy himself that goods equivalent to the value of remittance have been imported. AD should ensure that all import remittances outstanding on the notified date of IDPMS are uploaded in IDPMS (Import Data Processing and Monitoring System).

(iii) **Mode of payment:** A person resident in India may make payment for import of goods in foreign exchange through-

- an **international card** held by him/in rupees from international credit card/ debit card through the credit/debit card servicing bank in India against the charge slip signed by the importer, or
- as **prescribed by Reserve Bank** from time to time,

provided that the transaction is in conformity with the extant provisions and the import is in conformity with the Foreign Trade Policy in force.

In essence, payment has to be made through banking channels.

(iv) **Other modes:** For following transactions, a person resident in India may also make payment as under:

- (a) **In rupees** towards meeting expenses on account of boarding, lodging and services

related thereto or travel to and from and within India of a person resident outside India who is on a visit to India;

- (b) **By means of a crossed cheque or a draft** as consideration for purchase of gold or silver in any form imported by such person in accordance with the terms and conditions imposed under any order issued by the Central Government under the Foreign Trade (Development and Regulations) Act, 1992 or under any other law, rules or regulations for the time being in force;
- (c) **A company or resident in India may make payment in rupees** to its non-whole time director who is resident outside India and is on a visit to India for the company's work and is entitled to payment of sitting fees or commission or remuneration, and travel expenses to and from and within India, in accordance with the provisions contained in the company's Memorandum of Association or Articles of Association or in any agreement entered into it or in any resolution passed by the company in general meeting or by its Board of Directors. This is also subject to compliance with requirement of any law, rules, regulations, directions applicable for making such payments.

(4) Time Limit for Settlement of Import Payments:

(i) Time limit for Normal Imports:

- (a) In terms of the extant regulations, remittances against imports should be completed not later than six months from the date of shipment, except in cases where amounts are withheld towards guarantee of performance, etc.
- (b) AD may permit settlement of import dues delayed due to disputes, financial difficulties, etc. However, interest if any, on such delayed payments, usance bills (a bill of exchange which allows the drawee to have period of credit or term) or overdue interest is payable only for a period of up to three years from the date of shipment at the rate prescribed for trade credit from time to time.

- (ii) **Time Limit for Deferred Payment Arrangements:** Any deferred payment arrangements (including suppliers' and buyers' credit) entered into, for up to three years in case of import of capital goods and up to one year or the operating cycle whichever is less, in case of import of non-capital goods, shall be treated as trade credits for which the procedural guidelines as laid down in the Master Direction on External Commercial Borrowings, Trade Credits and Structured Obligations may be followed.

(5) Extension of Time:

- (i) **limit of extension:** AD can consider granting extension of time for settlement of import dues up to a period of six months at a time (maximum up to the period of three years) irrespective of the invoice value for delays on account of disputes about quantity or quality or non-fulfilment of terms of contract; financial difficulties and cases where

importer has filed suit against the seller. In cases where sector specific guidelines have been issued by Reserve Bank of India for extension of time (i.e. rough, cut and polished diamonds), the same will be applicable.

- (ii) **Circumstances:** While granting extension of time, AD must ensure that:
 - a. **The import transactions covered by the invoices are not under investigation** by Directorate of Enforcement / Central Bureau of Investigation or other investigating agencies;
 - b. While considering extension beyond one year from the date of shipment, the **total outstanding of the importer does not exceed USD one million or 10 per cent of the average import remittances** during the preceding two financial years, whichever is lower; and
 - c. Where extension of time has been granted by the AD, **the date up to which extension has been granted may be indicated** in the 'Remarks' column.
 - (iii) **In exceptional cases:** Cases not covered by the above instructions / beyond the above limits, may be referred to the concerned Regional Office of Reserve Bank of India.
 - (iv) **Noting of the extension:** The above extension period shall be reported in IDPMS as per message "Bill of Entry Extension" and the date up to which extension is granted will be indicated in "Extension Date" column.
- (6) **Import of Foreign Exchange / Indian Rupees:**
- (i) Except as otherwise provided in the Regulations, no person shall, without the general or special permission of the Reserve Bank, import or bring into India, any foreign currency. Import of foreign currency, including cheques, is governed by Section 6(3)(g) of the Foreign Exchange Management Act, 1999, and the Foreign Exchange Management (Export and Import of Currency) Regulations 2000.
 - (ii) Reserve Bank may allow a person to bring into India currency notes of Government of India and / or of Reserve Bank subject to such terms and conditions as the Reserve Bank may stipulate.
- (7) **Import of Foreign Exchange into India:** A person may–
- (i) **Send into India**, without limit, foreign exchange in any form (other than currency notes, bank notes and travelers cheques);
 - (ii) **Bring into India** from any place outside India, without limit, foreign exchange (other than unissued notes), subject to the condition that such person makes, on arrival in India, a declaration to the Custom Authorities at the Airport in the Currency Declaration Form (CDF) annexed to these Regulations;

Provided further that it shall not be necessary to make such declaration where the aggregate value of the foreign exchange in the form of currency notes, bank notes or travelers cheques brought in by such person at any one time does not exceed USD 10,000 (US Dollars ten thousand) or its equivalent and/or the aggregate value of foreign currency notes (cash portion) alone brought in by such person at any one time does not exceed USD 5,000 (US Dollars five thousand) or its equivalent.

(8) Import of Indian Currency and Currency Notes

- (i) Any person resident in India who had gone out of India on a temporary visit, may bring into India at the time of his return from any place outside India (**other than from Nepal and Bhutan**), currency notes of Government of India and Reserve Bank of India notes up to an amount not exceeding ` 25,000 (Rupees twenty five thousand only).
- (ii) **A person may bring into India from Nepal or Bhutan**, currency notes of Government of India and Reserve Bank of India for any amount in denominations up to `100/-.

(9) Issue of Guarantees by an Authorised Dealer:

- (i) An authorised dealer may give a **guarantee in respect of any debt, obligation or other liability incurred by a person resident in India and owed to a person resident outside India**, as an importer, in respect of import on deferred payment terms in accordance with the approval by the Reserve Bank of India for import on such terms.
- (ii) An authorised dealer may give **guarantee, Letter of Undertaking or Letter of Comfort in respect of any debt, obligation or other liability incurred by a person resident in India and owed to a person resident outside India** (being an overseas supplier of goods, bank or a financial institution), for import of goods, as permitted under the Foreign Trade Policy announced by Government of India from time to time and subject to such terms and conditions as may be specified by Reserve Bank of India from time to time.
- (iii) An authorised dealer may, **in the ordinary course of his business, give a guarantee in favour of a non-resident service provider**, on behalf of a resident customer who is a service importer, subject to such terms and conditions as stipulated by Reserve Bank of India from time to time:

Limit of providing guarantee:

Service importer	Amount of guarantee
Where a service importer is other than a Public Sector Company or a Department / Undertaking of the Government of India / State Government:	no guarantee for an amount exceeding USD 500,000 or its equivalent shall be issued

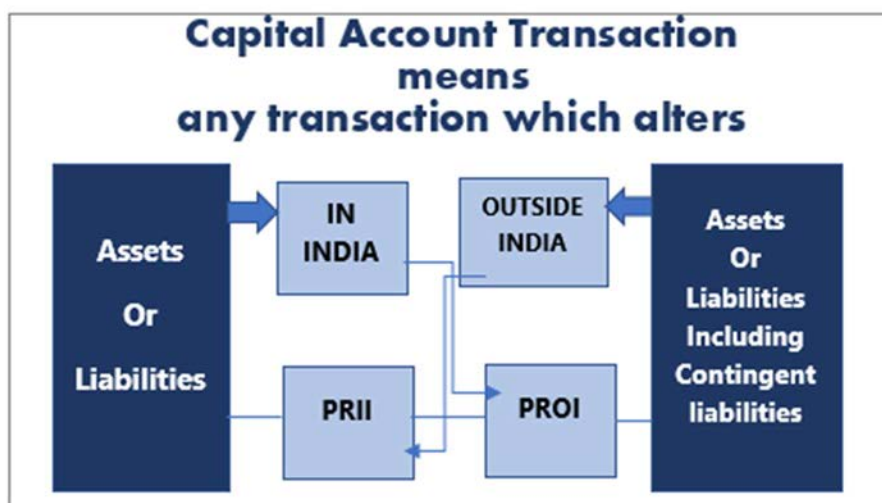
Where the service importer is a Public Sector Company or a Department / Undertaking of the Government of India / State Government	no guarantee for an amount exceeding USD 100,000 or its equivalent shall be issued without the prior approval of the Ministry of Finance, Government of India.

- (iv) An authorised dealer may, subject to the directions issued by the Reserve Bank of India in this behalf, permit a person resident in India to **issue corporate guarantee in favour of an overseas lessor** for financing import through operating lease effected in conformity with the Foreign Trade Policy in force and under the provisions of the Foreign exchange Management (Current Account Transactions) Rules, 2000, and the Directions issued by Reserve Bank of India under Foreign Exchange Management Act, 1999 from time to time.

❖ Capital account transactions [Section 6]

The definitions of “Capital Account Transactions” and its opposite “current account transactions” are contained in clauses (e) and (j) of Section 2. The regulations under FEMA apply to a transaction based on whether the transaction is “Capital Account Transaction” or a “Current Account Transaction”. These transactions broadly outline the basics and whole approach of the Act. Basically these two transactions have to be understood as being similar to the concepts of items relating to the profit and loss account or revenue items (with respect to current account transactions) and of Balance Sheet or capital items (with respect to capital account transactions).

Capital Account Transactions means “A transaction which alters the assets or liabilities including contingent liabilities outside India of persons resident in India or assets or liabilities in India of persons resident outside India would be a capital account transaction.”



Capital Accounts Transaction in India can be carried out only to the extent permitted because Indian Rupee is not yet fully convertible. Capital and current account transactions are intended to be mutually exclusive. **A transaction which alters the asset or liabilities in India of non-residents falls under the category of capital account.** However, as far as residents are concerned **transactions which alter the contingent liabilities outside India are also capital account transactions.** The Reserve Bank of India may by regulations place restrictions on various specified capital account transactions. **In simple terms, cross border transactions pertaining to investments, loans, immovable property, transfer of assets are Capital Account Transactions.**

- (1) Subject to the provisions of sub-section (2), any person may **sell or draw foreign exchange to or from an authorised person** for a capital account transaction.
- (2) Reserve Bank had the **power to specify the Capital Account transactions which are permitted and the relevant limits, terms and conditions.** By Finance Act 2015, powers for regulation of Capital Account Transactions for Non-debt instruments were transferred to Central Government. RBI continued to have powers to regulate debt instruments. The amendments have however been made effective from 15th October 2019. Now the regulations are as under:

The Reserve Bank may, in consultation with the Central Government, specify:

- (a) any class or classes of capital account transactions, involving debt instruments, which are permissible;
- (b) the limit up to which foreign exchange shall be admissible for such transactions;
- (c) any conditions which may be placed on such transactions;

Provided that the Reserve Bank or the Central Government shall not impose any restrictions on the drawal of foreign exchange for payment due on account of amortisation of loans or for depreciation of direct investments in the ordinary course of business.

RBI has issued notification for Debt instruments specifying the terms and conditions. These regulations for foreign investment in debt instruments. For investment by Indian residents outside India, RBI continues to have power to regulate the transactions for equity and debt.

- (2A) The Central Government may, in consultation with the Reserve Bank, prescribe— (a) any class or classes of capital account transactions, not involving debt instruments, which are permissible; (b) the limit up to which foreign exchange shall be admissible for such transactions; and (c) any conditions which may be placed on such transactions.

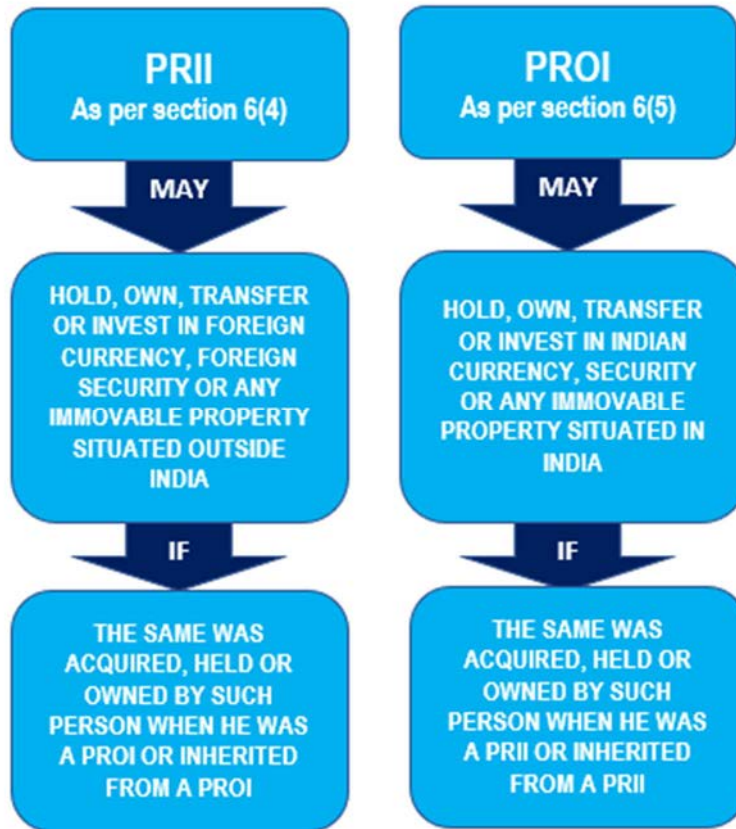
Central Government has issued notification for Non-debt instruments specifying the terms and conditions. RBI has issued notification for mode of payment and reporting of Non-debt instruments.

- (3) Before 15th October 2019, Section 6(3) specified a list of capital account transactions which could be regulated by RBI [apart from the general powers which it had under Section 6(2)]. **This list has now been deleted from 15th October 2019.**
- (4) **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.**

The RBI vide A.P. (DIR Series) Circular No. 90 dated 9th January, 2014 has issued a clarification on section 6(4) of the Act. This circular clarifies that section 6(4) of the Act covers the following transactions:

- (i) Foreign currency accounts opened and maintained by such a person when he was resident outside India;
 - (ii) Income earned through employment or business or vocation outside India taken up or commenced which such person was resident outside India, or from investments made while such person was resident outside India, or from gift or inheritance received while such a person was resident outside India;
 - (iii) Foreign exchange including any income arising therefrom, and conversion or replacement or accrual to the same, held outside India by a person resident in India acquired by way of inheritance from a person resident outside India.
 - (iv) A person resident in India may freely utilize all their eligible assets abroad as well as income on such assets or sale proceeds thereof received after their return to India for making any payments or to make any fresh investments abroad without approval of Reserve Bank, provided the cost of such investments and/or any subsequent payments received therefor are met exclusively out of funds forming part of eligible assets held by them and the transactions is not in contravention to extant FEMA provisions.
- (5) **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 a such person **when he was resident in India or inherited from a person who was resident in India.**
- (6) Without prejudice to the provisions of this section, the Reserve Bank may, by regulation, prohibit, restrict, or regulate establishment in India of a branch, office or other place of business by a person resident outside India, for carrying on any activity relating to such branch, office or other place of business.

Capital Account Transactions [Sec. 6(4) & 6(5)]



- (7) For the purposes of this section, the term “**debt instruments**” shall mean, such instruments as may be determined by the Central Government in consultation with the Reserve Bank.

A capital account transaction as stated earlier is a transaction, which alters the assets or liabilities, including contingent liabilities, outside India of persons resident in India or assets or liabilities in India of persons resident outside India would be a capital account transaction. The section gives a liberty by providing that any person may sell or draw foreign exchange to or from an authorised person for capital account transactions. However, the liberty to do so is subject to the provisions of sub-section (2) and (2A), which states that the Reserve Bank and the Central Government may specify class or classes of capital account transactions, which are permissible limit upto, which the foreign exchange shall be admissible for such transactions and the conditions which may be placed on such transactions.

Capital account transaction is basically split into the following categories under **Foreign Exchange Management (Permissible capital account transactions) Regulations, 2000**:-

- (I) transaction, which are permissible in respect of persons resident in India and outside India.

- (II) transaction on which restrictions cannot be imposed; and
- (III) transactions, which are prohibited.

I. Permissible Transactions

Under Sub-section (2) of Section 6, the RBI has issued the Foreign Exchange Management (Permissible Capital Account Transactions) Regulations, 2000. The Regulations specify the list of transaction, which are permissible in respect of persons resident in India in Schedule-I and the classes of capital account transactions of persons resident outside India in Schedule-II.

Further, subject to the provisions of the Act or the rules or regulations or direction or orders made or issued thereunder, any person may sell or draw foreign exchange to or from an authorised person for a capital account transaction specified in the Schedules; provided that the transaction is within the limit, if any, specified in the regulations relevant to the transaction.

SCHEDULE I

The list of permissible classes of transactions made by **persons resident in India** is:

- (a) Investment by a person resident in India in foreign securities.
- (b) Foreign currency loans raised in India and abroad by a person resident in India.
- (c) Transfer of immovable property outside India by a person resident in India.
- (d) Guarantees issued by a person resident in India in favour of a person resident outside India.
- (e) Export, import and holding of currency/currency notes.
- (f) Loans and overdrafts (borrowings) by a person resident in India from a person resident outside India.
- (g) Maintenance of foreign currency accounts in India and outside India by a person resident in India.
- (h) Taking out of insurance policy by a person resident in India from an insurance company outside India.
- (i) Loans and overdrafts by a person resident in India to a person resident outside India.
- (j) Remittance outside India of capital assets of a person resident in India.
- (k) Undertake derivative contracts

SCHEDULE II

The list of permissible classes of transactions made by **persons resident outside India** is:

- (a) Investment in India by a person resident outside India, that is to say,
 - (i) issue of security by a body corporate or an entity in India and investment therein by a person resident outside India; and

- (ii) investment by way of contribution by a person resident outside India to the capital of a firm or a proprietorship concern or an association of a person in India.
- (b) Acquisition and transfer of immovable property in India by a person resident outside India.
- (c) Guarantee by a person resident outside India in favour of, or on behalf of, a person resident in India.
- (d) Import and export of currency/currency notes into/from India by a person resident outside India.
- (e) Deposits between a person resident in India and a person resident outside India.
- (f) Foreign currency accounts in India of a person resident outside India.
- (g) Remittance outside India of capital assets in India of a person resident outside India.
- (h) Undertake derivative contracts

Transactions with no restriction

They are:

- (1) For amortisation of loan and
- (2) For depreciation of direct investments in ordinary course of business.

Also, restrictions cannot be imposed when drawal is of the purpose of repayments of loan installments.

Prohibited Transactions

On certain transactions, the Reserve Bank of India imposes prohibition.

- (a) no person shall **undertake or sell or draw foreign exchange to or from an authorised person** for any capital account transaction,

provided that-

- (i) subject to the provisions of the Act or the rules or regulations or directions or orders made or issued thereunder, **a resident individual may, draw from an authorized person foreign exchange not exceeding USD 250,000 per financial year or such amount as decided by Reserve Bank** from time to time for a capital account transaction specified in Schedule I.

Explanation: Drawal of foreign exchange as per item number 1 of Schedule III to Foreign Exchange Management (Current Account Transactions) Rules, 2000 dated 3rd May 2000 as amended from time to time, shall be subsumed within the limit under proviso (a) above.

- (ii) Where the **drawal of foreign exchange** by a resident individual for any capital account transaction specified in Schedule I **exceeds USD 250,000 per financial year, or as**

decided by Reserve Bank from time to time as the case may be, the limit specified in the regulations relevant to the transaction shall apply with respect to such drawal.

Provided further that no part of the foreign exchange of USD 250,000, drawn under proviso (a) shall be used for remittance directly or indirectly to countries notified as non-co-operative countries and territories by Financial Action Task Force (FATF) from time to time and communicated by the Reserve Bank of India to all concerned.

- (b) The **person resident outside India is prohibited from making investments in India** in any form, in any company, or partnership firm or proprietary concern or any entity whether incorporated or not which is engaged or proposes to engage:
- (i) In **the business of chit fund**; Registrar of Chits or an officer authorised by the state government in this behalf, may, in consultation with the State Government concerned, permit any chit fund to accept subscription from Non-resident Indians. Non- resident Indians shall be eligible to subscribe, through banking channel and on non- repatriation basis, to such chit funds, without limit subject to the conditions stipulated by the Reserve Bank of India from time to time.
 - (ii) As **Nidhi company**;
 - (iii) In **agricultural or plantation activities**;
 - (iv) In **real estate business, or construction of farm houses or**
 Explanation: In "real estate business" the term shall not include development of townships, construction of residential /commercial premises, roads or bridges and Real Estate Investment Trusts (REITs) registered and regulated under the SEBI (REITs) Regulations 2014.; or
 - (v) In **trading in Transferable Development Rights (TDRs).**

'Transferable Development Rights' means certificates issued in respect of category of land acquired for public purpose either by Central or State Government in consideration of surrender of land by the owner without monetary compensation, which are transferable in part or whole;

- (c) **No person resident in India shall undertake** any capital account transaction which is not permissible in terms of Order S.O. 1549(E) dated April 21, 2017, as amended from time to time, of the Government of India, Ministry of External Affairs, **with any person who is, a citizen of or a resident of Democratic People's Republic of Korea, or an entity incorporated or otherwise, in Democratic People's Republic of Korea**, until further orders, unless there is specific approval from the Central Government to carry on any transaction.
- (d) The **existing investment transactions, with any person** who is, a citizen of or resident of Democratic People's Republic of Korea, or an entity incorporated or otherwise in Democratic People's Republic of Korea, or any existing representative office or other assets possessed in

Democratic People's Republic of Korea, **by a person resident in India**, which is not permissible in terms of Order S.O. 1549(E) dated April 21, 2017, as amended from time to time, of the Government of India, Ministry of External Affairs **shall be closed/ liquidated/disposed/settled within a period of 180 days from the date of issue of this Notification**, unless there is specific approval from the Central Government to continue beyond that period.”

Thus, a capital account transaction is permitted only if it is specifically permitted under the regulations. If the transaction is not stated as generally permitted, a prior specific approval is required.

Framework for raising loans through External Commercial Borrowings: Transactions on account of External Commercial Borrowings (ECB) are governed by section 6(3)(d) of FEMA. ECBs are commercial loans raised by eligible resident entities from recognised non-resident entities and should conform to parameters such as minimum maturity, permitted and non-permitted end-uses, maximum all-in-cost ceiling, etc. The para-meters apply in totality and not on a stand-alone basis.

The term **‘All-in-Cost’** includes rate of interest, other fees, expenses, charges, guarantee fees whether paid in foreign currency or Indian Rupees (INR) but will not include commitment fees, pre-payment fees / charges, withholding tax payable in INR.

In the case of fixed rate loans, the swap cost plus spread should not be more than the floating rate plus the applicable spread. Additionally, for FCCBs, the issue related expenses should not exceed 4 per cent of the issue size and in case of private placement, these expenses should not exceed 2 per cent of the issue size, etc.

Approval route: Under the ECB framework, ECB can be raised either under the automatic route or under the approval route. Under the approval route, the prospective borrowers are required to send their requests to the Reserve Bank through their AD Banks for examination.

Automatic route: For the automatic route, the cases are examined by the Authorised Dealer Category-I (AD Category-I) banks.

ECB Framework: The framework for raising loans through ECB (hereinafter referred to as the ECB Framework) comprises the following two options:

Sr. No.	Parameters	⁴ FCY denominated ECB	INR denominated ECB
I	Currency of borrowing	Any freely convertible Foreign Currency	Indian Rupee (INR)
li	Forms of ECB	Loans including bank loans; floating/ fixed rate notes/ bonds/ debentures (other than fully and compulsorily convertible instruments); Trade	Loans including bank loans; floating/ fixed rate notes/bonds/ debentures/ preference shares (other than fully and compulsorily

⁴Foreign Currency

		credits beyond 3 years; ⁵ FCCBs; ⁶ FCEBs and Financial Lease.	convertible instruments); Trade credits beyond 3 years; and Financial Lease. Also, plain vanilla Rupee denominated bonds issued overseas, which can be either placed privately or listed on exchanges as per host country regulations.
iii	Eligible borrowers	All entities eligible to receive FDI. Further, the following entities are also eligible to raise ECB: i. Port Trusts; ii. Units in SEZ iii. SIDBI; and iv. EXIM Bank of India.	a) All entities eligible to raise FCY ECB; and b) Registered entities engaged in micro-finance activities, viz., registered Not for Profit companies, registered societies/trusts/cooperatives and Non-Government Organisations.
iv	Recognised lenders	The lender should be resident of FATF or ⁷ IOSCO compliant country, including on transfer of ECB. However, a) Multilateral and Regional Financial Institutions where India is a member country will also be considered as recognised lenders; b) Individuals as lenders can only be permitted if they are foreign equity holders or for subscription to bonds/debentures listed abroad; and c) Foreign branches / subsidiaries of Indian banks are permitted as recognised lenders only for FCY ECB (except FCCBs and FCEBs). Foreign branches / subsidiaries of Indian banks, subject to	

⁵Foreign Currency Convertible Bond: It refers to foreign currency denominated instruments which are issued in accordance with the Issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depositary Receipt Mechanism) Scheme, 1993, as amended from time to time. Issuance of FCCBs shall also conform to other applicable regulations. Further, FCCBs should be without any warrants attached.

⁶Foreign Currency Exchangeable Bonds (FCEBs): It refers to foreign currency denominated instruments which are issued in accordance with the Issue of Foreign Currency Exchangeable Bonds Scheme, 2008, as amended from time to time. FCEBs are exchangeable into equity share of another company, to be called the Offered Company, in any manner, either wholly, or partly or on the basis of any equity related warrants attached to debt instruments. Issuance of FCEBs shall also conform to other applicable regulations.

⁷IOSCO Compliant Country: A country whose securities market regulator is a signatory to the International Organisation of Securities Commission's (IOSCO's) Multilateral Memorandum of Understanding (Appendix A Signatories) or a signatory to bilateral Memorandum of Understanding with the SEBI for information sharing arrangements.

		applicable prudential norms, can participate as arrangers/ underwriters/market-makers/traders for Rupee denominated Bonds issued overseas. However, underwriting by foreign branches/subsidiaries of Indian banks for issuances by Indian banks will not be allowed.																		
v	Minimum Average Maturity Period (MAMP)	MAMP for ECB will be 3 years. Call and put options, if any, shall not be exercisable prior to completion of minimum average maturity. However, for the specific categories mentioned below, the MAMP will be as prescribed therein: <table> <tr> <th>Sr.No.</th><th>Category</th><th>MAMP</th></tr> <tr> <td>(a)</td><td>ECB raised by manufacturing companies up to USD 50 million or its equivalent per financial year.</td><td>1 year</td></tr> <tr> <td>(b)</td><td>ECB raised from foreign equity holder for working capital purposes, general corporate purposes or for repayment of Rupee loans</td><td>5 years</td></tr> <tr> <td>(c)</td><td>ECB raised by other than foreign equity holder for: (i) working capital purposes or general corporate purposes (ii) on-lending by NBFCs for working capital purposes or general corporate purposes</td><td>10 years</td></tr> <tr> <td>(d)</td><td>ECB raised by other than foreign equity holder for: (i) repayment of Rupee loans availed domestically for capital expenditure (ii) on-lending by NBFCs for the same purpose</td><td>7 years</td></tr> <tr> <td>(e)</td><td>ECB raised for (i) repayment of Rupee loans availed domestically for purposes other than capital expenditure (ii) on-lending by NBFCs for the same purpose</td><td>10 years</td></tr> </table> for the categories mentioned at (b) to (e) – (i) ECB cannot be raised from foreign branches / subsidiaries of Indian banks (ii) the prescribed MAMP will have to be strictly complied with under all circumstances.	Sr.No.	Category	MAMP	(a)	ECB raised by manufacturing companies up to USD 50 million or its equivalent per financial year.	1 year	(b)	ECB raised from foreign equity holder for working capital purposes, general corporate purposes or for repayment of Rupee loans	5 years	(c)	ECB raised by other than foreign equity holder for: (i) working capital purposes or general corporate purposes (ii) on-lending by NBFCs for working capital purposes or general corporate purposes	10 years	(d)	ECB raised by other than foreign equity holder for: (i) repayment of Rupee loans availed domestically for capital expenditure (ii) on-lending by NBFCs for the same purpose	7 years	(e)	ECB raised for (i) repayment of Rupee loans availed domestically for purposes other than capital expenditure (ii) on-lending by NBFCs for the same purpose	10 years
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vi	All-in-cost ceiling per annum	⁸ Benchmark rate plus 500 bps spread.	Benchmark rate plus 450 bps
vii	Other costs	Prepayment charge/ Penal interest, if any, for default or breach of covenants, should not be more than 2 per cent over and above the contracted rate of interest on the outstanding principal amount and will be outside the all-in-cost ceiling.	
viii	End-uses (Negative list)	The negative list, for which the ECB proceeds cannot be utilised, would include the following: a) Real estate activities. b) Investment in capital market. c) Equity investment. d) Working capital purposes, except in case of ECB mentioned at v(b) and v(c) above. e) General corporate purposes, except in case of ECB mentioned at v(b) and v(c) above. f) Repayment of Rupee loans, except in case of ECB mentioned at v(d) and v(e) above. g) On-lending to entities for the above activities, except in case of ECB raised by NBFCs as given at v(c), v(d) and v(e) above.	
ix	Exchange rate	Change of currency of FCY ECB into INR ECB can be at the exchange rate prevailing on the date of the agreement for such change between the parties concerned or at an exchange rate, which is less than the rate prevailing on the date of the agreement, if consented to by the ECB lender.	For conversion to Rupee, the exchange rate shall be the rate prevailing on the date of settlement.
x	Hedging provision	The entities raising ECB are required to follow the guidelines for hedging issued, if any, by the concerned sectoral or prudential regulator in	Overseas investors are eligible to hedge their exposure in Rupee through permitted derivative products with AD Category I

⁸Benchmark rate: Benchmark rate in case of FCY ECB/TC refers to 6-months LIBOR rate of different currencies or any other 6-month interbank interest rate applicable to the currency of borrowing, for eg., EURIBOR. Henceforth, benchmark rate in case of FCY ECB/TC shall refer to any widely accepted interbank rate or alternative reference rate (ARR) of 6-month tenor, applicable to the currency of borrowing.

		respect of foreign currency exposure. Infrastructure space companies shall have a Board approved risk management policy. Further, such companies are required to mandatorily hedge 70 per cent of their ECB exposure in case the average maturity of the ECB is less than 5 years. The designated AD Category-I bank shall verify that 70 per cent hedging requirement is complied with during the currency of the ECB and report the position to RBI through Form ECB 2. The following operational aspects with respect to hedging should be ensured: a. Coverage: The ECB borrower will be required to cover the principal as well as the coupon through financial hedges. The financial hedge for all exposures on account of ECB should start from the time of each such exposure (i.e. the day the liability is created in the books of the borrower). b. Tenor and rollover: A minimum tenor of one year for the financial hedge would be required with periodic rollover, duly ensuring that the exposure on account of ECB is not unhedged at any point during the currency of the ECB. c. Natural Hedge: Natural hedge, in lieu of financial	banks in India. The investors can also access the domestic market through branches / subsidiaries of Indian banks abroad or branches of foreign banks with Indian presence on a back to back basis.

		hedge, will be considered only to the extent of offsetting projected cash flows / revenues in matching currency, net of all other projected outflows. For this purpose, an ECB may be considered naturally hedged if the offsetting exposure has the maturity/cash flow within the same accounting year. Any other arrangements/structures, where revenues are indexed to foreign currency will not be considered as a natural hedge.	
xi	Change of currency of borrowing	Change of currency of ECB from one freely convertible foreign currency to any other freely convertible foreign currency as well as to INR is freely permitted.	Change of currency from INR to any freely convertible foreign currency is not permitted.
Note: The ECB framework is not applicable in respect of investments in Non-Convertible Debentures in India made by Registered Foreign Portfolio Investors. Lending and borrowing under the ECB framework by Indian banks and their branches/subsidiaries outside India will be subject to prudential guidelines issued by the Department of Banking Regulation of the Reserve Bank. Further, other entities raising ECB are required to follow the guidelines issued, if any, by the concerned sectoral or prudential regulator.			

Limit and leverage: Under the aforesaid framework, all eligible borrowers can raise ECB up to USD 750 million or equivalent per financial year under the automatic route. Further, in case of FCY denominated ECB raised from direct foreign equity holder, ECB liability-equity ratio for ECB raised under the automatic route cannot exceed 7:1. However, this ratio will not be applicable if the outstanding amount of all ECB, including the proposed one, is up to USD 5 million or its equivalent. Further, the borrowing entities will also be governed by the guidelines on debt equity ratio, issued, if any, by the sectoral or prudential regulator concerned.

Issuance of Guarantee, etc. by Indian banks and Financial Institutions: Issuance of any type of guarantee by Indian banks, All India Financial Institutions and NBFCs relating to ECB is not permitted. Further, financial intermediaries (viz., Indian banks, All India Financial Institutions, or NBFCs) shall not invest in FCCBs/ FCEBs in any manner whatsoever.

Parking of ECB proceeds: ECB proceeds are permitted to be parked abroad as well as domestically in the manner given below:

Parking of ECB proceeds abroad:	Parking of ECB proceeds domestically:
ECB proceeds meant only for foreign currency expenditure can be parked abroad pending utilisation. Till utilisation, these funds can be invested in the following liquid assets: - deposits or Certificate of Deposit or other products offered by banks rated not less than AA (-) by Standard and Poor/Fitch IBCA or Aa3 by Moody's; - Treasury bills and other monetary instruments of one-year maturity having minimum rating as indicated above and - deposits with foreign branches/subsidiaries of Indian banks abroad.	ECB proceeds meant for Rupee expenditure should be repatriated immediately for credit to their Rupee accounts with AD Category I banks in India. ECB borrowers are also allowed to park ECB proceeds in term deposits with AD Category I banks in India for a maximum period of 12 months cumulatively. These term deposits should be kept in unencumbered position.

Procedure of raising ECB: All ECB can be raised under the automatic route if they conform to the parameters prescribed under this framework. For approval route cases, the borrowers may approach the RBI with an application in prescribed format (Form ECB) for examination through their AD Category I bank. Such cases shall be considered keeping in view the overall guidelines, macroeconomic situation and merits of the specific proposals. ECB proposals received in the Reserve Bank above certain threshold limit (refixed from time to time) would be placed before the Empowered Committee set up by the Reserve Bank. The Empowered Committee will have external as well as internal members and the Reserve Bank will take a final decision in the cases taking into account recommendation of the Empowered Committee. Entities desirous to raise ECB under the automatic route may approach an AD Category I bank with their proposal along with duly filled in Form ECB.

Reporting Requirements: Borrowings under ECB Framework are subject to following reporting requirements apart from any other specific reporting required under the framework:

- Loan Registration Number (LRN):** Any draw-down in respect of an ECB should happen only after obtaining the LRN from the Reserve Bank. To obtain the LRN, borrowers are required to submit duly certified Form ECB, which also contains terms and conditions of the ECB, in duplicate to the designated AD Category I bank. In turn, the AD Category I bank will forward one copy to the Director, Reserve Bank of India, Department of Statistics and Information Management, External Commercial Borrowings Division, Bandra-Kurla Complex, Mumbai – 400

051 (Contact numbers 022-26572513 and 022-26573612). Copies of loan agreement for raising ECB are not required to be submitted to the Reserve Bank.

2. **Changes in terms and conditions of ECB:** Changes in ECB parameters in consonance with the ECB norms, including reduced repayment by mutual agreement between the lender and borrower, should be reported to the DSIM through revised Form ECB at the earliest, in any case not later than 7 days from the changes effected. While submitting revised Form ECB the changes should be specifically mentioned in the communication.
3. **Monthly Reporting of actual transactions:** The borrowers are required to report actual ECB transactions through Form ECB 2 Return through the AD Category I bank on monthly basis so as to reach DSIM within seven working days from the close of month to which it relates. Changes, if any, in ECB parameters should also be incorporated in Form ECB 2 Return.
4. **Late Submission Fee (LSF) for delay in reporting:** Any borrower, who is otherwise in compliance of ECB guidelines, can regularise the delay in reporting of drawdown of ECB proceeds before obtaining LRN or delay in submission of Form ECB/ Form ECB 2 returns, by payment of late submission fees.
5. **Standard Operating Procedure (SOP) for Untraceable Entities:** The following SOP has to be followed by designated AD Category-I banks in case of untraceable entities who are found to be in contravention of reporting provisions for ECB by failing to submit prescribed return(s) under the ECB framework, either physically or electronically, for past eight quarters or more.
 - i. **Definition:** Any borrower who has raised ECB will be treated as 'untraceable entity', if entity/auditor(s)/director(s)/ promoter(s) of entity are not reachable/responsive/reply in negative over email/letters/phone for a period of not less than two quarters with documented communication/ reminders numbering 6 or more and it fulfills both of the following conditions:
 - (a) Entity not found to be operative at the registered office address as per records available with the AD Bank or not found to be operative during the visit by the officials of the AD Bank or any other agencies authorised by the AD bank for the purpose;
 - (b) Entities have not submitted Statutory Auditor's Certificate for last two years or more;
 - ii. **Action:** The followings actions are to be undertaken in respect of 'untraceable entities':
 - (a) File Revised Form ECB, if required, and last Form ECB 2 Return without certification from company with 'UNTRACEABLE ENTITY' written in bold on top. The outstanding amount will be treated as written-off from external debt liability of the country but may be retained by the lender in its books for recovery through judicial/ non-judicial means;

- (b) No fresh ECB application by the entity should be examined/processed by the AD bank;
- (c) Directorate of Enforcement should be informed whenever any entity is designated 'UNTRACEABLE ENTITY'; and
- (d) No inward remittance or debt servicing will be permitted under auto route.

6. **Powers delegated to AD Category I banks to deal with ECB cases:** The designated AD Category I banks can approve any requests from the borrowers for changes in respect of ECB, except for FCCBs/FCEBs, duly ensuring that the changed conditions, including change in name of borrower/lender, transfer of ECB and any other parameters, comply with extant ECB norms and are with the consent of lender(s). Further, the following can also be undertaken under the automatic route:

- (I) **Change of the AD Category I bank:** AD Category I bank can be changed subject to obtaining no objection certificate from the existing AD Category I bank.
- (II) **Cancellation of LRN:** The designated AD Category I banks may directly approach DSIM for cancellation of LRN for ECB contracted, subject to ensuring that no draw down against the said LRN has taken place and the monthly ECB-2 returns till date in respect of the allotted LRN have been submitted to DSIM.
- (III) **Refinancing of existing ECB:** Refinancing of existing ECB by fresh ECB provided the outstanding maturity of the original borrowing (weighted outstanding maturity in case of multiple borrowings) is not reduced and all-in-cost of fresh ECB is lower than the all-in-cost (weighted average cost in case of multiple borrowings) of existing ECB. Further, refinancing of ECB raised under the previous ECB frameworks may also be permitted, subject to additionally ensuring that the borrower is eligible to raise ECB under the extant framework. Raising of fresh ECB to part refinance the existing ECB is also permitted subject to same conditions. Indian banks are permitted to participate in refinancing of existing ECB, only for highly rated corporates (AAA) and for Maharatna/Navratna public sector undertakings.
- (IV) **Conversion of ECB into equity:** Conversion of ECB, including those which are matured but unpaid, into equity is permitted subject to the following conditions:
 - i. The activity of the borrowing company is covered under the automatic route for FDI or Government approval is received, wherever applicable, for foreign equity participation as per extant FDI policy.
 - ii. The conversion, which should be with the lender's consent and without any additional cost, should not result in contravention of eligibility and breach of applicable sector cap on the foreign equity holding under FDI policy;

- iii. Applicable pricing guidelines for shares are complied with;
 - iv. In case of partial or full conversion of ECB into equity, the reporting to the Reserve Bank will be as under:
 - (a) For partial conversion, the converted portion is to be reported in Form FC-GPR prescribed for reporting of FDI flows, while monthly reporting to DSIM in Form ECB 2 Return will be with suitable remarks, viz., "ECB partially converted to equity".
 - (b) For full conversion, the entire portion is to be reported in Form FC-GPR, while reporting to DSIM in Form ECB 2 Return should be done with remarks "ECB fully converted to equity". Subsequent filing of Form ECB 2 Return is not required.
 - (c) For conversion of ECB into equity in phases, reporting through Form FC-GPR and Form ECB 2 Return will also be in phases.
 - v. If the borrower concerned has availed of other credit facilities from the Indian banking system, including foreign branches/subsidiaries of Indian banks, the applicable prudential guidelines issued by the Department of Banking Regulation of Reserve Bank, including guidelines on restructuring are complied with;
 - vi. Consent of other lenders, if any, to the same borrower is available or atleast information regarding conversions is exchanged with other lenders of the borrower.
 - vii. For conversion of ECB dues into equity, the exchange rate prevailing on the date of the agreement between the parties concerned for such conversion or any lesser rate can be applied with a mutual agreement with the ECB lender. It may be noted that the fair value of the equity shares to be issued shall be worked out with reference to the date of conversion only.
- (V) **Security for raising ECB:** AD Category I banks are permitted to allow creation/cancellation of charge on immovable assets, movable assets, financial securities and issue of corporate and/or personal guarantees in favour of overseas lender / security trustee, to secure the ECB to be raised/ raised by the borrower, subject to satisfying themselves that:
- (i) the underlying ECB is in compliance with the extant ECB guidelines,
 - (ii) there exists a security clause in the Loan Agreement requiring the ECB borrower to create/cancel charge, in favour of overseas lender/security trustee, on immovable assets/movable assets/financial securities/issuance of corporate and/or personal guarantee, and
 - (iii) No objection certificate, as applicable, from the existing lenders in India has been obtained in case of creation of charge.

Once the aforesaid stipulations are met, the AD Category I bank may permit creation of charge on immovable assets, movable assets, financial securities and issue of corporate and/or personal guarantees, during the currency of the ECB with security co-terminating with underlying ECB, **subject to the following:**

- i. **Creation of Charge on Immovable Assets:** The arrangement shall be subject to the following:
 - (a) Such security shall be subject to provisions contained in the Foreign Exchange Management (Acquisition and Transfer of Immovable Property in India) Regulations, 2017, as amended from time to time.
 - (b) The permission should not be construed as a permission to acquire immovable asset (property) in India, by the overseas lender/ security trustee.
 - (c) In the event of enforcement / invocation of the charge, the immovable asset/ property will have to be sold only to a person resident in India and the sale proceeds shall be repatriated to liquidate the outstanding ECB.
- ii. **Creation of Charge on Movable Assets:** In the event of enforcement/ invocation of the charge, the claim of the lender, whether the lender takes over the movable asset or otherwise, will be restricted to the outstanding claim against the ECB. Encumbered movable assets may also be taken out of the country subject to getting 'No Objection Certificate' from domestic lender/s, if any.
- iii. **Creation of Charge over Financial Securities:** The arrangements may be permitted subject to the following:
 - (a) Pledge of shares of the borrowing company held by the promoters as well as in domestic associate companies of the borrower is permitted. Pledge on other financial securities, viz. bonds and debentures, Government Securities, Government Savings Certificates, deposit receipts of securities and units of the Unit Trust of India or of any mutual funds, standing in the name of ECB borrower/promoter, is also permitted.
 - (b) In addition, security interest over all current and future loan assets and all current assets including cash and cash equivalents, including Rupee accounts of the borrower with ADs in India, standing in the name of the borrower/ promoter, can be used as security for ECB. The Rupee accounts of the borrower/promoter can also be in the form of escrow arrangement or debt service reserve account.
 - (c) In case of invocation of pledge, transfer of financial securities shall be in accordance with the extant FDI/FII policy including provisions relating to sectoral cap and pricing as applicable read with the Foreign Exchange

Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2017, as amended from time to time.

- iv. **Issue of Corporate or Personal Guarantee:** The arrangement shall be subject to the following:
- (a) A copy of Board Resolution for the issue of corporate guarantee for the company issuing such guarantee, specifying name of the officials authorised to execute such guarantees on behalf of the company or in individual capacity should be obtained.
 - (b) Specific requests from individuals to issue personal guarantee indicating details of the ECB should be obtained.
 - (c) Such security shall be subject to provisions contained in the Foreign Exchange Management (Guarantees) Regulations, 2000, as amended from time to time.
 - (d) ECB can be credit enhanced / guaranteed / insured by overseas party/ parties only if it/ they fulfil/s the criteria of recognised lender under extant ECB guidelines.

7. Additional Requirements: While exercising the delegated powers, the AD Category I banks should ensure that:

- (i) The changes permitted are in conformity with the applicable ceilings / guidelines and the ECB continues to be in compliance with applicable guidelines. It should also be ensured that if the ECB borrower has availed of credit facilities from the Indian banking system, including foreign branches/subsidiaries of Indian banks, any extension of tenure of ECB (whether matured or not) shall be subject to applicable prudential guidelines issued by Department of Banking Regulation of Reserve Bank including guidelines on restructuring.
- (ii) The changes in the terms and conditions of ECB allowed by the ADs under the powers delegated and / or changes approved by the Reserve Bank should be reported to the DSIM as given at paragraph 2 above. Further, these changes should also get reflected in the Form ECB 2 returns appropriately.

8. Special Dispensations under the ECB framework:

1. **ECB facility for Oil Marketing Companies:** Notwithstanding the provisions contained in “End uses”, “Hedging Provision” and “Limit and Leverage” above, Public Sector Oil Marketing Companies (OMCs) can raise ECB for working capital purposes with minimum average maturity period of 3 years from all recognised lenders under the automatic route without mandatory hedging and individual limit requirements. The overall ceiling for such ECB shall be USD 10 billion or equivalent. However, OMCs should have a Board approved forex mark to market procedure and prudent risk management policy, for such ECB. All other provisions under the ECB framework will be applicable to such ECB.

2. **ECB facility for Startups:** AD Category-I banks are permitted to allow Startups to raise ECB under the automatic route as per the following framework:
- (i) **Eligibility:** An entity recognised as a Startup by the Central Government as on date of raising ECB.
 - (ii) **Maturity:** Minimum average maturity period will be 3 years.
 - (iii) **Recognised lender:** Lender / investor shall be a resident of a FATF compliant country. However, foreign branches/subsidiaries of Indian banks and overseas entity in which Indian entity has made overseas direct investment as per the extant Overseas Direct Investment Policy will not be considered as recognised lenders under this framework.
 - (iv) **Forms:** The borrowing can be in form of loans or non-convertible, optionally convertible or partially convertible preference shares.
 - (v) **Currency:** The borrowing should be denominated in any freely convertible currency or in Indian Rupees (INR) or a combination thereof. In case of borrowing in INR, the non-resident lender, should mobilise INR through swaps/outright sale undertaken through an AD Category-I bank in India.
 - (vi) **Amount:** The borrowing per Startup will be limited to USD 3 million or equivalent per financial year either in INR or any convertible foreign currency or a combination of both.
 - (vii) **All-in-cost:** Shall be mutually agreed between the borrower and the lender.
 - (viii) **End uses:** For any expenditure in connection with the business of the borrower.
 - (ix) **Conversion into equity:** Conversion into equity is freely permitted subject to Regulations applicable for foreign investment in Startups.
 - (x) **Security:** The choice of security to be provided to the lender is left to the borrowing entity. Security can be in the nature of movable, immovable, intangible assets (including patents, intellectual property rights), financial securities, etc. and shall comply with foreign direct investment / foreign portfolio investment / or any other norms applicable for foreign lenders / entities holding such securities. Further, issuance of corporate or personal guarantee is allowed. Guarantee issued by a non-resident(s) is allowed only if such parties qualify as lender under ECB for Startups. However, issuance of guarantee, standby letter of credit, letter of undertaking or letter of comfort by Indian banks, all India Financial Institutions and NBFCs is not permitted.
 - (xi) **Hedging:** The overseas lender, in case of INR denominated ECB, will be eligible to hedge its INR exposure through permitted derivative products with AD Category – I banks in India. The lender can also access the domestic market through branches/subsidiaries of Indian banks abroad or branches of foreign bank with Indian presence on a back to back basis.

Note: Startups raising ECB in foreign currency, whether having natural hedge or not, are exposed to currency risk due to exchange rate movements and hence are advised to ensure that they have an appropriate risk management policy to manage potential risk arising out of ECB.

- (xii) **Conversion rate:** In case of borrowing in INR, the foreign currency - INR conversion will be at the market rate as on the date of agreement.
- (xiii) **Other Provisions:** Other provisions like parking of ECB proceeds, reporting arrangements, powers delegated to AD banks, borrowing by entities under investigation, conversion of ECB into equity will be as included in the ECB framework. However, provisions on leverage ratio and ECB liability: Equity ratio will not be applicable. Further, the Start-ups as defined in "Eligibility" above as well as other start-ups which do not comply with the aforesaid definition but are eligible to receive FDI, can also raise ECB under the general ECB route/framework.

9. Borrowing by Entities under Investigation: All entities against which investigation / adjudication / appeal by the law enforcing agencies for violation of any of the provisions of the Regulations under FEMA pending, may raise ECB as per the applicable norms, if they are otherwise eligible, notwithstanding the pending investigations / adjudications / appeals, without prejudice to the outcome of such investigations / adjudications / appeals. The borrowing entity shall inform about pendency of such investigation / adjudication / appeal to the AD Category-I bank / RBI as the case may be. Accordingly, in case of all applications where the borrowing entity has indicated about the pending investigations / adjudications / appeals, the AD Category I Banks / Reserve Bank while approving the proposal shall intimate the agencies concerned by endorsing a copy of the approval letter.

10. ECB by entities under restructuring/ ECB facility for refinancing stressed assets:

1. An entity which is under a restructuring scheme/ corporate insolvency resolution process can raise ECB only if specifically permitted under the resolution plan.
2. Eligible corporate borrowers who have availed Rupee loans domestically for capital expenditure in manufacturing and infrastructure sector and which have been classified as SMA-2 or NPA can avail ECB for repayment of these loans under any one time settlement with lenders. Lender banks are also permitted to sell, through assignment, such loans to eligible ECB lenders, provided, the resultant external commercial borrowing complies with all-in-cost, minimum average maturity period and other relevant norms of the ECB framework. Foreign branches/ overseas subsidiaries of Indian banks are not eligible to lend for the above purposes. The applicable MAMP will have to be strictly complied with under all circumstances.
3. Eligible borrowers under the ECB framework, who are participating in the Corporate Insolvency Resolution Process under Insolvency and Bankruptcy Code, 2016 as resolution applicants, can raise ECB from all recognised lenders, except foreign branches/subsidiaries of Indian banks,

for repayment of Rupee term loans of the target company. Such ECB will be considered under the approval route, procedure of which is given at "Procedure of raising ECB" above.

11. **Dissemination of information:** For providing greater transparency, information with regard to the name of the borrower, amount, purpose and maturity of ECB under both Automatic and Approval routes are put on the RBI's website, on a monthly basis, with a lag of one month to which it relates.
12. **Compliance with the guidelines:** The primary responsibility for ensuring that the borrowing is in compliance with the applicable guidelines is that of the borrower concerned. Any contravention of the applicable provisions of ECB guidelines will invite penal action under the FEMA. The designated AD Category I bank is also expected to ensure compliance with applicable ECB guidelines by their constituents.

OVERSEAS INVESTMENTS BY RESIDENTS: Vide Notification G.S.R. 646(E) dated 22 August 2022, through Ministry of Finance, in exercise of the powers conferred under the Foreign Exchange Management Act, 1999 and in supersession of the Foreign Exchange Management (Transfer or Issue of Any Foreign Security) Regulations, 2004 and the Foreign Exchange Management (Acquisition and Transfer of Immovable Property Outside India) Regulations, 2015, except as respects things done or omitted to be done before such supersession, the Central Government hereby makes the Foreign Exchange Management (Overseas Investment) Rules, 2022 and the Foreign Exchange Management (Overseas Investment) Regulations, 2022.

Said Notification, combined the FEMA (Transfer or Issue of Foreign Security) Regulations, 2004 ('erstwhile ODI regulations') and FEMA (Acquisition and Transfer of immovable property outside India) Regulations, 2015 into FEMA (Overseas Investment) Rules, 2022 ('OI Rules') and FEMA (Overseas Investment) Regulations, 2022 ('OI Regulations') and the erstwhile regulations stand superseded.

To provide clarity to said Rules and Regulations, RBI has also issued Foreign Exchange Management (Overseas Investment) Directions, 2022 on 22 August 2022 ('OI Directions'). It's giving effect to the above, in supersession of the erstwhile Master Directions on Direct Investment by Residents in Joint Venture ('JV') / Wholly Owned Subsidiary ('WOS') abroad.

In view of the evolving needs of businesses in India, in an increasingly integrated global market, there is need of Indian corporates to be part of global value chain. The revised regulatory framework for overseas investment provides for simplification of the existing framework for overseas investment and has been aligned with the current business and economic dynamics. Clarity on Overseas Direct Investment and Overseas Portfolio Investment has been brought in and various overseas investment related transactions that were earlier under approval route are now under automatic route, significantly enhancing "Ease of Doing Business".

Scope:

Overseas Investment Rules	Overseas Investment Regulations
lay down the regulatory framework for making overseas investment	provide only the operational part for making overseas investment
It emphasize on the permissions, conditions for making overseas investment, restrictions from making Overseas Direct Investment ('ODI') and Overseas Portfolio Investment, pricing guidelines, transfer, liquidation and restructuring of ODI. While the OI Rules have been framed by CG, however, the same will be administered by the RBI.	It emphasize on providing of conditions for undertaking Financial Commitment, investment in debt instruments, consideration in case of acquisition or transfer of equity capital of a Foreign Entity, mode of payment, obligations of Persons Resident in India, reporting requirements, consequence of delay in reporting and restrictions on further FC/ transfer.

OVERSEAS INVESTMENT RULES, 2022**Definitions– Significant definitions:**

1. **“control”** means the right to appoint majority of the directors or to control management or policy decisions exercisable by a person or persons acting individually or in concert, directly or indirectly, including by virtue of their shareholding or management rights or shareholders' agreements or voting agreements that entitle them to ten per cent. or more of voting rights or in any other manner in the entity [Regulation 2(1)(c)]
2. **“disinvestment”** means partial or full extinguishment of right, title or possession of equity capital acquired under these rules [Regulation 2(1)(d)]
3. **“equity capital”** means equity shares or perpetual capital or instruments that are irredeemable or contribution to non-debt capital of a foreign entity in the nature of fully and compulsorily convertible instruments [Regulation 2(1)(e)]
4. **“financial commitment”** means the aggregate amount of investment made by a person resident in India by way of Overseas Direct Investment, debt other than Overseas Portfolio Investment in a foreign entity or entities in which the Overseas Direct Investment is made and shall include the non fund-based facilities extended by such person to or on behalf of such foreign entity or entities [Regulation 2(1)(f)]
5. **“financial service regulator”** means a financial service regulator established under any law in force in India and include the Reserve Bank, the Securities and Exchange Board of India, the Insurance Regulatory and Development Authority and the Pension Fund Regulatory and Development Authority [Regulation 2(1)(g)]

6. **“foreign entity”** means an entity formed or registered or incorporated outside India, including International Financial Services Centre that has limited liability:

Provided that the restriction of limited liability shall not apply to an entity with core activity in a strategic sector; [Regulation 2(1)(h)]

“strategic sector” shall include energy and natural resources sectors such as oil, gas, coal, mineral ores, submarine cable system and start-ups and any other sector or sub-sector as deemed necessary by the Central Government; [Regulation 2(1)(z)]

7. **“host country”** or **“host jurisdiction”** means the country or jurisdiction, including the International Financial Services Centre, in which the foreign entity is formed, registered or incorporated, as the case may be [Regulation 2(1)(i)]

8. **“Indian entity”** means–

- (i) a company defined under the Companies Act, 2013
- (ii) a body corporate incorporated by any law for the time being in force;
- (iii) a Limited Liability Partnership duly formed and incorporated under the Limited Liability Partnership Act, 2008 (6 of 2009); and
- (iv) a partnership firm registered under the Indian Partnership Act, 1932 (9 of 1932). [Regulation 2(1)(j)]

9. **“listed foreign entity”** means a foreign entity whose equity shares or any other fully and compulsorily convertible instrument is listed on a recognised stock exchange outside India; [Regulation 2(1)(m)]

10. **“listed Indian company”** means an Indian company that has equity shares or any of its fully and compulsorily convertible instruments listed on a recognised stock exchange in India and the expression “unlisted Indian company” shall be construed accordingly [Regulation 2(1)(n)]

11. **“Overseas Direct Investment”** or “ODI” means investment by way of acquisition of unlisted equity capital of a foreign entity, or subscription as a part of the memorandum of association of a foreign entity, or investment in ten per cent, or more of the paid-up equity capital of a listed foreign entity or investment with control where investment is less than ten per cent. of the paid-up equity capital of a listed foreign entity;

Explanation– For the purposes of this clause, where an investment by a person resident in India in the equity capital of a foreign entity is classified as ODI, such investment shall continue to be treated as ODI even if the investment falls to a level below ten per cent. of the paid-up equity capital or such person loses control in the foreign entity [Regulation 2(1)(q)]

12. **“Overseas Investment”** or “OI” means financial commitment and Overseas Portfolio Investment by a person resident in India [Regulation 2(1)(r)]

13. **“Overseas Portfolio Investment”** or “OPI” means investment, other than ODI, in foreign securities, but not in any unlisted debt instruments or any security issued by a person resident in India who is not in an IFSC:

Provided that OPI by a person resident in India in the equity capital of a listed entity, even after its delisting shall continue to be treated as OPI until any further investment is made in the entity.

Explanation– For the purposes of this clause, the expression “debt instruments” means the instruments specified as such in clause (A) of rule 5 [Regulation 2(1)(s)]

14. **“relative”** shall have the same meaning as assigned to it in clause (77) of section 2 of the Companies Act, 2013, [Regulation 2(1)(t)]
15. **“resident individual”** means a person resident in India who is a natural person; [Regulation 2(1)(u)]
16. **“Resident Foreign Currency Account” or “RFC Account”** shall have the same meaning as assigned to it in the Foreign Exchange Management (Foreign Currency Accounts by a Person Resident in India) Regulations, 2015 [Regulation 2(1)(v)]
17. **“Subsidiary” or “step down subsidiary”** of a foreign entity means an entity in which the foreign entity has control [Regulation 2(1)(y)]
18. **“sweat equity shares”** means such equity shares as are issued by an overseas entity to its directors or employees at a discount or for consideration other than cash, for providing their know-how or making available rights like intellectual property rights or value additions, by whatever name called [Regulation 2(za)]

Non-Applicability of Rules and Regulations relating thereto in Certain Cases. Nothing in these rules or the Foreign Exchange Management (Overseas Investment) Regulations, 2022 shall apply to–

- (a) any **investment made outside India by a financial institution** in an IFSC;
- (b) **acquisition or transfer of any investment outside India** made,–
- (i) out of **Resident Foreign Currency Account**; or
 - (ii) out of **foreign currency resources held outside India** by a person who is employed in India for a specific duration irrespective of length thereof or for a specific job or assignment, duration of which does not exceed three years; or
 - (iii) in accordance with **sub-section (4) of section 6** of the Act.

Explanation.– For the purposes of this rule, the expression “financial institution” shall have the same meaning as assigned to it in the International Financial Services Centre’s Authority Act, 2019 (50 of 2019).

Debt instruments and non-debt instruments– The following shall be the debt instruments and non-debt instruments as determined by the Central Government, namely:–

(A) Debt instruments:	(B) Non-debt instruments:
Government bonds;	all investments in equity in incorporated entities (public, private, listed and unlisted);
corporate bonds;	capital participation in Limited Liability Partnerships;
all tranches of securitisation structure which are not equity tranche;	all instruments of investment as recognised in the Foreign Direct Investment policy from time to time;
borrowings by firms through loans; and	investment in units of Alternative Investment Funds and Real Estate Investment Trust and Infrastructure Investment Trusts;
depository receipts whose underlying securities are debt securities;	investment in units of mutual funds and Exchange-Traded Fund which invest more than fifty per cent in equity;
	the junior-most layer (i.e. equity tranche) of securitisation structure;
	acquisition, sale or dealing directly in immovable property;
	contribution to trusts; and
	depository receipts issued against equity instruments;

Continuity of certain investments – Any investment or financial commitment outside India made in accordance with the Act or the rules or regulations made thereunder and held as on the date of publication of these rules in the Official Gazette, shall be deemed to have been made under these rules and the Foreign Exchange Management (Overseas Investment) Regulations, 2022.

Rights issue and bonus shares–

- (1) **Holding of equity capital of foreign entity:** Any person resident in India who has acquired and continues to hold equity capital of any foreign entity in accordance with the provisions of the Act or the rules or regulations made thereunder–
 - (a) may invest in the equity capital issued by such entity as a rights issue; or
 - (b) may be granted bonus shares subject to the terms and conditions under these rules.
- (2) **Transfer of above rights:** The person resident in India acquiring the rights under sub-rule (1) may renounce such rights in favour of a person resident in India or a person resident outside India.

Prohibition on investment outside India– Save as otherwise provided in the Act or these rules or the regulations made or directions issued under the Act, **no person resident in India shall make or transfer any investment or financial commitment outside India.**

Overseas Investment–

- (1) **Investment in foreign entity engaged in bonafide business activity:** Save as otherwise provided in these rules or the Foreign Exchange Management (Overseas Investment) Regulations, 2022, any investment made outside India by a person resident in India shall be made in a foreign entity engaged in a bona fide business activity, directly or through step down subsidiary or the special-purpose vehicle, subject to the limits and the conditions laid down in these rules and the said regulations:

Structural requirements of a foreign entity: Provided that the structure of such subsidiary or step down subsidiary of the foreign entity shall comply with the structural requirements of a foreign entity:

When CG approval is required: Provided further that Overseas Investment or transfer of such investment including swap of securities in a foreign entity formed, registered or incorporated in Pakistan or in any other jurisdiction as may be advised by the Central Government from time to time shall require prior approval of the Central Government.

Explanation– For the purposes of this sub-rule, “**bonafide business activity**” shall mean any business activity permissible under any law in force in India and the host country or host jurisdiction, as the case may be:

- (2) Notwithstanding anything contained in these rules or Foreign Exchange Management (Overseas Investment) Regulations 2022 –
- (i) **Permit for Financial commitment in strategic sectors:** The Central Government may, on an application made to it through the Reserve Bank, permit financial commitment in strategic sectors or geographies, above the limits laid down in these rules and subject to such terms and conditions as it considers necessary.
 - (ii) **Permit PRII to make/transfer any investment/Financial commitment:** the Reserve Bank may, on an application made to it through the designated AD bank and for sufficient reasons, permit a person resident in India to make or transfer any investment or financial commitment outside India subject to such conditions as may be laid down by it:

Provided that Overseas Investment by a person resident in India shall not be made in a foreign entity located in a country or jurisdiction as may be decided by the Central Government from time to time.
- (3) The Reserve Bank, if it considers necessary may, in consultation with the Central Government–
- (i) **stipulate the ceiling for the aggregate outflows** during a financial year on account of financial commitment or Overseas Portfolio Investment;

- (ii) **stipulate the ceiling beyond which** the amount of financial commitment by a person resident in India in a financial year **shall require its prior approval**.

No Objection Certificate–

- (1) Any person resident in India who–

- (i) has an **account appearing as a non-performing asset**; or
- (ii) is classified **as a wilful defaulter** by any bank; or
- (iii) is **under investigation** by a financial service regulator or by investigative agencies in India, namely, the Central Bureau of Investigation or Directorate of Enforcement or Serious Frauds Investigation Office, shall, before making any financial commitment or undertaking disinvestment under these rules or the Foreign Exchange Management (Overseas Investment) Regulations, 2022, obtain a No Objection Certificate from the lender bank or regulatory body or investigative agency by making an application in writing to such bank or regulatory body or investigative agency concerned:

where there is failure to furnish the certificate: Provided that where the lender bank or regulatory body or investigative agency concerned fails to furnish the certificate within sixty days from the date of receipt of such application, it may be presumed that there was no objection to the proposed transaction.

- (2) The No Objection Certificate issued shall be addressed by the lender bank or regulatory body or investigative agency concerned to the **designated AD bank with an endorsement to the applicant**.

Manner of making overseas investment:

Investment by the body	Manner of overseas investment
Overseas Direct Investment by Indian entity	may make Overseas Direct Investment in the manner and subject to the terms and conditions prescribed in Schedule I.
Overseas Portfolio Investment by an Indian entity	may make Overseas Portfolio Investment in the manner and subject to the terms and conditions prescribed in Schedule II.
Overseas Investment by resident individual	may make Overseas Investment in the manner and subject to the terms and conditions prescribed in Schedule III
Overseas Investment by person resident in India other than Indian entity and resident Individual	may make Overseas Investment in the manner and subject to the terms and conditions prescribed in Schedule IV

Overseas Investment in IFSC by person resident in India	may make Overseas Investment in an IFSC in India in the manner and subject to the terms and conditions prescribed in Schedule V

Pricing guidelines – (1) the issue or transfer of equity capital of a foreign entity from a person resident outside India or a person resident in India to a person resident in India who is eligible to make such investment or from a person resident in India to a person resident outside India shall be subject to a price arrived on an arm's length basis.

- (2) The AD bank, before facilitating a transaction above, shall ensure compliance with arm's length pricing taking into consideration the valuation as per any internationally accepted pricing methodology for valuation.

Transfer or liquidation.

- (1) a person resident in India holding equity capital in accordance with these rules may transfer such investment, in compliance with the limits and subject to the conditions for such investment or disinvestment, pricing guidelines or documentation and reporting requirements, in the manner provided in these rules and the Foreign Exchange Management (Overseas Investment) Regulations, 2022.
- (2) A person resident in India may transfer equity capital by way of sale to a person resident in India, who is eligible to make such investment under these rules, or to a person resident outside India.
- (3) In case the transfer is on account of merger, amalgamation or demerger or on account of buyback of foreign securities, such transfer or liquidation in case of liquidation of the foreign entity, shall have the approval of the competent authority as per the applicable laws in India or the laws of the host country or host jurisdiction, as the case may be.
- (4) Where the disinvestment by a person resident in India pertains to ODI–
 - (i) the transferor, in case of full disinvestment other than by way of liquidation, shall not have any dues outstanding for receipt, which such transferor is entitled to receive from the foreign entity as an investor in equity capital and debt;
 - (ii) the transferor, in case of any disinvestment must have stayed invested for at least one year from the date of making ODI:

Provided that the above conditions shall not be applicable in case of a merger, demerger or amalgamation between two or more foreign entities that are wholly-owned, directly or indirectly, by the Indian entity or where there is no change or dilution in aggregate equity holding of the Indian entity in the merged or demerged or amalgamated entity.

- (5) The holding of any investment or transfer thereof in any manner shall not be permitted if the initial investment was not permitted under the Act.

Restructuring – A person resident in India who has made ODI in a foreign entity may permit restructuring of the balance sheet by such foreign entity, which has been incurring losses for the previous two years as evidenced by its last audited balance sheets, subject to ensuring compliance with reporting, documentation requirements and subject to the diminution in the total value of the outstanding dues towards such person resident in India on account of investment in equity and debt, after such restructuring not exceeding the proportionate amount of the accumulated losses:

Provided that in case of such diminution where the amount of corresponding original investment is more than USD 10 million or in the case where the amount of such diminution exceeds twenty per cent of the total value of the outstanding dues towards the Indian entity or investor, **the diminution in value shall be duly certified on an arm's length basis by a registered valuer as per the Companies Act, 2013 or corresponding valuer registered with the regulatory authority or certified public accountant** in the host jurisdiction:

Provided further that the **certificate dated not more than six months before the date of the transaction** shall be submitted to the designated AD bank.

Restrictions and prohibitions

- (1) **No person resident in India shall make ODI** in a foreign entity engaged in–
 - (a) real estate activity;
 - (b) gambling in any form; and
 - (c) dealing with financial products linked to the Indian rupee without specific approval of the Reserve Bank.

Explanation– For the purposes of this sub-rule, the expression "real estate activity" means buying and selling of real estate or trading in Transferable Development Rights but does not include the development of townships, construction of residential or commercial premises, roads or bridges for selling or leasing.

- (2) **Any ODI in start-ups recognised under the laws of the host country or host jurisdiction** as the case may be, shall be made by an Indian entity only from the internal accruals whether from the Indian entity or group or associate companies in India and in case of resident individuals, from own funds of such an individual.
- (3) **No person resident in India shall make financial commitment in a foreign entity that has invested or invests into India**, at the time of making such financial commitment or at any time thereafter, either directly or indirectly, resulting in a structure with more than two layers of subsidiaries:

Exception: Provided that such restriction shall not apply to the following classes of companies mentioned in sub-rule (2) of rule 2 of the Companies (Restriction on Number of Layers) Rules, 2017 as may be amended from time to time, namely:-

- (a) a banking company

- (b) a non-banking financial company which is registered with the Reserve Bank and considered as systematically important non-banking financial company by the Reserve Bank
- (c) an insurance company and
- (d) a Government company

Requirements for investment to be specified by Reserve Bank– The mode of payment, deferred payment of consideration, reporting, realisation, and other requirements for any investment outside India by a person resident in India shall be as per the regulations made in this behalf by the Reserve Bank under the Act.

Restriction on acquisition or transfer of immovable property outside India–

- (1) Save as otherwise provided in the Act or this rule, no person resident in India shall acquire or transfer any immovable property situated outside India **without general or special permission of the Reserve Bank:**

However, nothing contained in this rule shall apply to a property–

- (i) held by a person resident in India who is a national of a foreign State;
- (ii) acquired by a person resident in India on or before the 8th day of July, 1947 and continued to be held by such person with the permission of the Reserve Bank;
- (iii) acquired by a person resident in India on a lease not exceeding five years.

- (2) Notwithstanding anything contained in sub-rule (1)–

- (i) **a person resident in India may acquire immovable property outside India** by way of-
 - inheritance or
 - gift or
 - purchase from a person resident in India who has acquired such property as per the foreign exchange provisions in force at the time of such acquisition;
- (ii) Acquiring of immovable property outside India from a person resident outside India- a person resident in India may acquire immovable property outside India from a person resident outside India–
 - (a) by way of inheritance;
 - (b) by way of purchase out of foreign exchange held in RFC account;
 - (c) by way of purchase out of the remittances sent under the Liberalised Remittance Scheme instituted by the Reserve Bank:

Provided that such remittances under the Liberalised Remittance Scheme may be consolidated in respect of relatives if such relatives, being persons resident in India, comply with the terms and conditions of the Scheme;

- (d) jointly with a relative who is a person resident outside India;
- (e) out of the income or sale proceeds of the assets, other than ODI, acquired overseas under the provisions of the Act;
- (iii) **an Indian entity having an overseas office may acquire immovable property outside India** for the business and residential purposes of its staff, as per the directions issued by the Reserve Bank from time to time;
- (iv) **a person resident in India who has acquired any immovable property outside India** in accordance with the foreign exchange provisions in force at the time of such acquisition may—
 - (a) **transfer such property** by way of gift to a person resident in India who is eligible to acquire such property under these rules or by way of sale;
 - (b) **create a charge on such property** in accordance with the Act or the rules or regulations made thereunder or directions issued by the Reserve Bank from time to time.
- (3) The holding of any investment in immovable property or transfer thereof in any manner shall not be permitted if the initial investment in immovable property was not permitted under the Act.

Schedule I [See rule 11]

Manner of making Overseas Direct Investment by Indian entity

1. Manner of making ODI — (1) An Indian entity may make ODI by way of investment in equity capital for the purpose of undertaking bonafide business activity in the manner and subject to the limits and conditions provided in this Schedule.

- (2) The ODI may be made or held by way of—
 - (i) **subscription** as part of memorandum of association or purchase of equity capital, listed or unlisted;
 - (ii) **acquisition** through bidding or tender procedure;
 - (iii) **acquisition of equity capital** by way of rights issue or allotment of bonus shares;
 - (iv) **capitalisation**, within the time period, if any, specified for realisation under the Act, of any amount due towards the Indian entity from the foreign entity, the remittance of which is permitted under the Act or does not require prior permission of the Central Government or the Reserve Bank under the Act or any rules or regulations made or directions issued thereunder;

- (v) the **swap of securities**;
- (vi) **merger, demerger, amalgamation** or any scheme of arrangement as per the applicable laws in India or laws of the host country or the host jurisdiction, as the case may be.

2. **ODI in financial services activity –**

- (1) An **Indian entity engaged in financial services activity in India may make ODI** in a foreign entity, which is directly or indirectly engaged in financial services activity, subject to the following conditions, namely:--

- (i) the Indian entity has **posted net profits** during the preceding three financial years;
- (ii) the Indian entity is **registered with or regulated** by a financial services regulator in India;
- (iii) the Indian entity has **obtained approval** as may be required from the regulators of such financial services activity, **both in India and the host country or host jurisdiction**, as the case may be, for engaging in such financial services:

- (2) An **Indian entity not engaged in financial services activity in India may make ODI** in a foreign entity, which is directly or indirectly engaged in financial services activity [except banking or insurance] subject to the condition that such **Indian entity has posted net profits during the preceding three financial years:**

Provided that an Indian entity not engaged in the insurance sector may make ODI in general and health insurance where such insurance business is supporting the core activity undertaken overseas by such an Indian entity.

- (3) **If an Indian entity does not meet the net profits** required under sub paragraph (1) & (2) of this paragraph due to the impact of Covid-19 during the period from 2020-2021 to 2021-2022, then the financial results of such period may be excluded for considering the profitability period of three years:

Provided that such period may be extended by the Reserve Bank in consultation with the Central Government, as it may deem necessary:

- (4) **Overseas Investment by banks and non-banking financial institutions regulated by the Reserve Bank** shall be subject to the conditions laid down by the Reserve Bank under applicable laws in this regard.

3. Limit for financial commitment – (1) The total financial commitment made by an Indian entity in all the foreign entities taken together at the time of undertaking such commitment shall **not exceed 400 percent of its net worth** as on the date of the last audited balance sheet or as directed by the Reserve Bank, in consultation with Central Government from time to time.

- (2) The total financial commitment referred as above shall not include capitalisation of retained earnings for reckoning such limit but **shall include–**

- (i) **utilisation of the amount** raised by the issue of American Depository Receipts or Global Depository Receipts and stock-swap of such receipts; and
- (ii) **utilisation of the proceeds** from External Commercial Borrowings to the extent the corresponding pledge or creation of charge on assets to raise such borrowings has not already been reckoned towards the above limit:

Provided that the financial commitment made by Maharatna or Navratna or Miniratna or subsidiaries of such public sector undertakings in foreign entities outside India engaged in strategic sectors shall not be subject to the limits laid down under this paragraph.

Explanation.– For the purposes of this Schedule, a foreign entity shall be considered to be engaged in the business of financial services activity if it undertakes an activity, which if carried out by an entity in India, requires registration with or is regulated by a financial sector regulator in India.

Schedule II [See rule 12]

Manner of making Overseas Portfolio Investment (OPI) by an Indian entity

1. OPI by an Indian entity.–

- (1) An Indian entity may make OPI which shall **not exceed fifty percent of its net worth** as on the date of its last audited balance sheet, in the manner and subject to the conditions laid down in this Schedule.
- (2) A **listed Indian company may make OPI** including by way of reinvestment.
- (3) An **unlisted Indian entity may make OPI** only under clauses (iii), (iv), (v) and (vi) of subparagraph (2) of paragraph 1 of Schedule I.

Schedule III [See rule 13]

Manner of making Overseas Investment by resident individual

- 1. **Manner of making OI** – (1) Any resident individual may make ODI by way of investment in equity capital or OPI in the manner provided in this Schedule and unless otherwise provided hereunder, shall be subject to the overall ceiling under the Liberalised Remittance Scheme of the Reserve Bank.
- (2) A resident individual may make or hold Overseas Investment by way of–
 - (i) ODI in an operating foreign entity not engaged in financial services activity and which does not have subsidiary or step down subsidiary where the resident individual has control in the foreign entity;
 - (ii) OPI, including by way of reinvestment;
 - (iii) ODI or OPI, as the case may be, by way of–

- (a) capitalisation, within the time period, if any, specified for realisation under the Act, of any amount due from the foreign entity the remittance of which is permitted under the Act or does not require prior permission of the Central Government or the Reserve Bank;
- (b) swap of securities on account of a merger, demerger, amalgamation or liquidation;
- (c) acquisition of equity capital through rights issue or allotment of bonus shares;
- (d) gift as per the conditions laid down under this Schedule;
- (e) inheritance;
- (f) acquisition of sweat equity shares;
- (g) acquisition of minimum qualification shares issued for holding a management post in a foreign entity;
- (h) acquisition of shares or interest under Employee Stock Ownership Plan or Employee Benefits Scheme:

Provided that ODI in respect of clauses (e), (f), (g) and (h) may be made in a foreign entity whether or not such foreign entity is engaged in financial services activity or has subsidiary or step down subsidiary where the resident individual has control:

Provided further that the acquisition of less than ten per cent. of the equity capital, whether listed or unlisted, of a foreign entity without control under clauses (f), (g) and (h), shall be treated as OPI.

Explanation— For the purposes of this Schedule, a foreign entity will be considered to be engaged in the business of financial services activity if it undertakes an activity, which if carried out by an entity in India, requires registration with or is regulated by a financial sector regulator in India.

2. Acquisition by way of gift or inheritance – (1) A resident individual may, without any limit, acquire foreign securities by way of inheritance from a person resident in India who is holding such securities in accordance with the provisions of the Act or from a person resident outside India.

- (2) A resident individual, without any limit, may acquire foreign securities by way of gift from a person resident in India who is a relative and holding such securities in accordance with the provisions of the Act.
- (3) A resident individual may acquire foreign securities by way of gift from a person resident outside India in accordance with the provisions of the Foreign Contribution (Regulation) Act, 2010 and the rules and regulations made thereunder.

3. Acquisition of shares or interest under Employee Stock Ownership Plan or Employee Benefits Scheme or sweat equity shares:

- (1) A resident individual, who is an employee or a director of an office in India or branch of an overseas entity or a subsidiary in India of an overseas entity or of an Indian entity in which the overseas entity has direct or indirect equity holding-

may acquire, without limit, shares or interest under Employee Stock Ownership Plan or Employee Benefits Scheme or sweat equity shares offered by such overseas entity, provided that the issue of Employee Stock Ownership Plan or Employee Benefits Scheme are offered by the issuing overseas entity globally on a uniform basis.

Explanation.- For the purposes of this paragraph, the expression,-

- (i) "indirect equity holding" means indirect foreign equity holding through a special purpose vehicle or step down subsidiary;
 - (ii) "Employee Benefit Scheme" means any compensation or incentive given to the directors or employees of any entity which gives such directors or employees ownership interest in an overseas entity through ESOP or any similar scheme.
- (2) Notwithstanding anything contained in these rules, a resident individual may acquire Employee Stock Ownership Plans under any scheme of the Central Government.

Schedule IV [See rule 14]

Overseas Investment by person resident in India other than Indian entity and resident Individual

1. ODI by Registered Trust or Society – Any person being a registered Trust or a registered Society engaged in the educational sector or which has set up hospitals in India may make ODI in a foreign entity with the prior approval of the Reserve Bank, subject to the following conditions, namely:-

- (i) the foreign entity is engaged in the same sector that the Indian Trust or Society is engaged in;
- (ii) the Trust or the Society, as the case may be, should have been in existence for at least three financial years before the year in which such investment is being made;
- (iii) the trust deed in case of a Trust, and the memorandum of association or rules or bye-laws in case of a Society shall permit the proposed ODI;
- (iv) such investment have the approval of the trustees in case of a Trust and the governing body or council or managing or executive committee in case of a Society;
- (v) in case the Trust or the Society require special licence or permission either from the Ministry of Home Affairs, Central Government or from the relevant local authority, as the case may be, the special licence or permission has been obtained and submitted to the designated AD bank.

2. OI by Mutual Funds or Venture Capital Funds or Alternative Investment Funds.-

- (1) A mutual fund or Venture Capital Fund or Alternative Investment Fund may acquire or transfer foreign securities as stipulated by SEBI from time to time in accordance with the provisions of

these rules and subject to such other terms and conditions as may be laid down by the Reserve Bank and the SEBI under applicable laws from time to time:

Provided that the aggregate limit for such investment shall be decided by the Reserve Bank in consultation with the Central Government:

Provided further that the individual limits for such investments shall be as per the instructions issued by the SEBI from time to time.

- (2) Every transaction relating to the purchase and sale of foreign security by the funds referred to in sub- paragraph (1) shall be routed through the designated AD bank in India:
- (3) Notwithstanding anything contained in these rules, any investment under these rules by mutual funds, Venture Capital Funds and Alternative Investment Funds shall be treated as OPI.

Explanation – For the purposes of this paragraph, “Alternative Investment Fund” means any fund registered as such with the SEBI.

3. Opening of Demat Accounts by clearing corporations of stock exchanges and clearing members – Any person, being a SEBI approved clearing corporation of a stock exchange and its clearing members, may acquire, hold and transfer foreign securities, offered as collateral by foreign portfolio investors and, subject to the guidelines issued by the SEBI from time to time–

- (i) open and maintain Demat Account with foreign depositories;
- (ii) remit the proceeds arising due to such action, if any; and
- (iii) liquidate such foreign securities and repatriate the proceeds thereof to India.

4. Acquisition and transfer of foreign securities by domestic depository – A domestic depository may acquire, hold and transfer foreign securities of a foreign entity, being the underlying security to issue Indian Depository Receipts as may be authorised by such foreign entity or its overseas custodian bank and the person investing in Indian Depository Receipts may either sell or continue to hold foreign securities in accordance with the conditions provided in these rules and the Foreign Exchange Management (Overseas Investment) Regulations, 2022 upon conversion of such depository receipts.

5. Acquisition and transfer of foreign securities by AD bank – An AD bank including its overseas branch may acquire or transfer foreign securities in accordance with the terms of the host country or host jurisdiction, as the case may be, in the normal course of its banking business.

Schedule V [See rule 15]

Overseas Investment in IFSC by person resident in India

1. Overseas Investment in IFSC by person resident in India –

- (1) Subject to the provisions of these rules and the Foreign Exchange Management (Overseas Investment) Regulations, 2022, a person resident in India may make Overseas Investment in an IFSC in India within the limits provided in these rules.

- (2) A person resident in India may make Overseas Investment in an IFSC in the manner as laid down in Schedule I or Schedule II or Schedule III or Schedule IV: Provided that –
- (i) in the case of an ODI made in an IFSC, the approval by the financial services regulator concerned, wherever applicable, shall be decided within forty-five days from the date of application complete in all respects failing which it shall be deemed to be approved;
 - (ii) an Indian entity not engaged in financial services activity in India, making ODI in a foreign entity, which is directly or indirectly engaged in financial services activity, except banking or insurance, who does not meet the net profit condition as required under these rules, may make ODI in an IFSC.
 - (iii) a person resident in India may make contribution to an investment fund or vehicle set up in an IFSC as OPI;
 - (iv) a resident individual may make ODI in a foreign entity, including an entity engaged in financial services activity, (except in banking and insurance), in IFSC if such entity does not have subsidiary or step down subsidiary outside IFSC where the resident individual has control in the foreign entity.
- (3) A recognised stock exchange in the IFSC shall be treated as a recognised stock exchange outside India for the purpose of these rules.

Foreign Exchange Management (Overseas Investment) Regulations, 2022

Said regulations deals with various modes of operations of investments

Regulation 3 of the FEM (Overseas Investment) Regulations, 2022 deals with **the Financial commitment by Indian entity by modes other than equity capital–**

- (1) The Indian entity may lend or invest in any debt instrument issued by a foreign entity or extend non-fund based commitment to or on behalf of a foreign entity including overseas step down subsidiaries of such Indian entity subject to the following conditions within the financial commitment limit as prescribed in the Foreign Exchange Management (Overseas Investment) Rules, 2022:–
- (i) the Indian entity is eligible to make Overseas Direct Investment (ODI);
 - (ii) the Indian entity has made ODI in the foreign entity;
 - (iii) the Indian entity has acquired control in such foreign entity at the time of making such financial commitment.
- (2) The financial commitments under regulations 4, 5, 6 and 7 shall be reckoned towards the financial commitment limit referred to in sub-regulation (1).

Financial commitment by Indian entity by way of debt – Regulation 4 stated that **an Indian entity may lend or invest in any debt instruments** issued by a foreign entity subject to the

condition that such loans are duly backed by a loan agreement where the rate of interest shall be charged on an arm's length basis.

Explanation— For the purpose of this regulation, the expression “arm's length” means a transaction between two related parties that is conducted as if they were unrelated, so that there is no conflict of interest.

Financial commitment by way of guarantee – Regulation 5 states that-

- (1) The following guarantees may be issued to or on behalf of the foreign entity or any of its step down subsidiary in which the Indian entity has acquired control through the foreign entity, namely:-
 - (i) corporate or performance guarantee by such Indian entity;
 - (ii) corporate or performance guarantee by a group company of such Indian entity in India, being a holding company (which holds at least 51 per cent. stake in the Indian entity) or a subsidiary company (in which the Indian entity holds at least 51 per cent. stake) or a promoter group company, which is a body corporate;
 - (iii) personal guarantee by the resident individual promoter of such an Indian entity;
 - (iv) bank guarantee, which is backed by a counter-guarantee or collateral by the Indian entity or its group company as above, and issued, by a bank in India.
- (2) Where the guarantee is extended by a group company, it shall be counted towards the utilisation of its financial commitment limit independently and in case of a resident individual promoter, the same shall be counted towards the financial commitment limit of the Indian entity:

Provided that where the commitment under sub-regulation (1) is extended by a group company, any fund-based exposure to or from the Indian entity shall be deducted from the net worth of such group company for computing its financial commitment limit:

Provided further that where the guarantee under sub-regulation (1) is extended by a promoter, which is a body corporate or an individual, the Indian entity shall be a part of the promoter group.

Explanation – For the purposes of this sub-regulation, the expression “promoter group” shall have the meaning as assigned to it in the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations 2018.
- (3) No guarantee shall be open-ended.
- (4) The guarantee, to the extent of the amount invoked, shall cease to be a part of the non-fund based commitment but be considered as lending.
- (5) Where a guarantee has been extended jointly and severally by two or more Indian entities, 100 per cent. of the amount of such guarantee shall be reckoned towards the individual limits of each of such Indian entities.

- (6) In case of performance guarantee, 50 per cent. of the amount of guarantee shall be reckoned towards the financial commitment limit.
- (7) Roll-over of guarantee shall not be treated as fresh financial commitment where the amount on account of such roll-over does not exceed the amount of original guarantee.

Financial commitment by way of pledge or charge,- As per regulation 6, an Indian entity, which has made ODI by way of investment in equity capital in a foreign entity, may—

- (a) **pledge the equity capital of the foreign entity** in which it has made ODI or of its step down subsidiary outside India, held directly by the Indian entity in a foreign entity and indirectly in step down subsidiary, in favour of an AD bank or a public financial institution in India or an overseas lender, for availing fund based or non-fund based facilities for itself or for any foreign entity in which it has made ODI or its step down subsidiaries outside India or in favour of a debenture trustee registered with SEBI for availing fund based facilities for itself;
- (b) **create charge** by way of mortgage, pledge, hypothecation or any other identical mode on—
 - (i) **its assets in India**, including the assets of its group company or associate company, promoter or director, in favour of an AD bank or a public financial institution in India or an overseas lender as security for availing of the fund based or non-fund based facility or both, for any foreign entity in which it has made ODI or for its step down subsidiary outside India; or
 - (ii) **the assets outside India of the foreign entity** in which it has made ODI or of its step down subsidiary outside India in favour of an AD bank in India or a public financial institution in India as security for availing of the fund based or non-fund based facility or both, for itself or any foreign entity in which it has made ODI or for its step down subsidiary outside India or in favour of a debenture trustee registered with SEBI in India for availing fund based facilities for itself;

Provided that—

- (i) the **value of the pledge or charge or the amount of the facility, whichever is less**, shall be reckoned towards the financial commitment limit in force at the time of such pledge or charge provided such facility has not already been reckoned towards such limit and excluding cases where the facility has been availed by the Indian entity for itself;
- (ii) **overseas lender** in whose favour there is such a pledge or charge **shall not be from any country or jurisdiction in which financial commitment is not permissible** under the Foreign Exchange Management (Overseas Investment) Rules, 2022;
- (iii) the **creation or enforcement of such pledge or charge shall be in accordance with the provisions of the Act or rules or regulations** made or directions issued thereunder.

Explanation – For the purposes of this regulation–

- (i) the expression “public financial institution” shall have the same meaning as assigned to it under clause (72) of section 2 of the Companies Act, 2013 (18 of 2013);
- (ii) the “negative pledge” or “negative charge” created by an Indian entity or a bid bond guarantee obtained in accordance with these regulations for participation in a bidding or tender procedure for the acquisition of a foreign entity shall not be reckoned towards the financial commitment limit referred to in sub-regulation (1) of regulation 3.

Acquisition or transfer by way of deferred payment – As per Regulation 7-

- (1) Where a person resident in India acquires equity capital by way of subscription to an issue or by way of purchase from a person resident outside India or where a person resident outside India acquires equity capital by way of purchase from a person resident in India, and where such equity capital is reckoned as ODI, the payment of amount of consideration for the equity capital acquired may be deferred for such definite period from the date of the agreement as provided in such agreement subject to the following terms and conditions, namely:–

- (i) the foreign securities equivalent to the amount of total consideration shall be transferred or issued, as the case may be, upfront by the seller to the buyer;
- (ii) the full consideration finally paid shall be compliant with the applicable pricing guidelines:

Provided that the deferred part of the consideration in case of acquisition of equity capital of a foreign entity by a person resident in India shall be treated as non-fund based commitment.

- (2) The buyer may be indemnified by the seller up to such amount and be subject to such terms and conditions as may be mutually agreed upon and laid down in the agreement:

Provided that such agreement is in compliance with the provisions of the Act and the rules and regulations made thereunder.

Mode of payment. – Regulation 8 specifies that a person resident in India making Overseas Investment may make payment –

- (i) by remittance made through banking channels;
- (ii) from funds held in an account maintained in accordance with the provisions of the Act;
- (iii) by swap of securities;
- (iv) by using the proceeds of American Depository Receipts or Global Depository Receipts or stock swap of such receipts or external commercial borrowings raised in accordance with the provisions of the Act and the rules and regulations made thereunder for making ODI or financial commitment by way of debt by an Indian entity.

Obligations of person resident in India – In accordance with Regulation 9 following are the obligations of person resident in India:

- (1) A person resident in India acquiring equity capital in a foreign entity, which is reckoned as ODI, shall submit to the AD bank share certificates or any other relevant documents as per the applicable laws of the host country or the host jurisdiction, as the case may be, as an evidence of such investment in the foreign entity within six months from the date of effecting remittance or the date on which the dues to such person are capitalised or the date on which the amount due was allowed to be capitalised, as the case may be.
- (2) A person resident in India, through its designated AD bank, shall obtain a Unique Identification Number or "UIN" from the Reserve Bank for the foreign entity in which the ODI is intended to be made before sending outward remittance or acquisition of equity capital in a foreign entity, whichever is earlier.
- (3) A person resident in India making ODI shall designate an AD bank and route all transactions relating to a particular UIN through such AD:

Provided that where more than one person resident in India makes financial commitment in the same foreign entity, all such persons shall route all transactions relating to that UIN through the AD bank designated for that UIN.

- (4) A person resident in India having ODI in a foreign entity, wherever applicable, shall realise and repatriate to India, all dues receivable from the foreign entity with respect to investment in such foreign entity, the amount of consideration received on account of transfer or disinvestment of such ODI and the net realisable value of the assets on account of the liquidation of the foreign entity as per the laws of the host country or the host jurisdiction, as the case may be, within ninety days from the date when such receivables fall due or the date of such transfer or disinvestment or the date of the actual distribution of assets made by the official liquidator.
- (5) A person resident in India who is eligible to make ODI may make remittance towards earnest money deposit or obtain a bid bond guarantee from an AD bank for participation in bidding or tender procedure for the acquisition of a foreign entity:

Provided that in case of an open-ended bid bond guarantee, it shall be converted into a close-ended guarantee not later than three months from the date of award of the contract.

Reporting requirements for Overseas Investment– According to Regulation 10 following are the reporting requirements:

- (1) Unless otherwise provided in these regulations, all reporting by a person resident in India, as specified, shall be made through the designated AD bank in the manner provided in this regulation and in the format provided by the Reserve Bank.
- (2) A person resident in India who has made ODI or making financial commitment or undertaking disinvestment in a foreign entity shall report the following, namely:–

- (a) financial commitment, whether it is reckoned towards the financial commitment limit or not, at the time of sending outward remittance or making a financial commitment, whichever is earlier;
 - (b) disinvestment within thirty days of receipt of disinvestment proceeds; (c) restructuring within thirty days from the date of such restructuring.
- (3) A person resident in India other than a resident individual making any Overseas Portfolio Investment (OPI) or transferring such OPI by way of sale shall report such investment or transfer of investment within sixty days from the end of the half-year in which such investment or transfer is made as of September or March-end:

Provided that in case of OPI by way of acquisition of shares or interest under Employee Stock Ownership Plan or Employee Benefits Scheme, the reporting shall be done by the office in India or branch of an overseas entity or a subsidiary in India of an overseas entity or the Indian entity in which the overseas entity has direct or indirect equity holding where the resident individual is an employee or director.

- (4) A person resident in India acquiring equity capital in a foreign entity which is reckoned as ODI, shall submit an Annual Performance Report (APR) with respect to each foreign entity every year by 31st December and where the accounting year of such foreign entity ends on 31st December, the APR shall be submitted by 31st December of the next year:

Provided that no such reporting shall be required where—

- (i) a person resident in India is holding less than 10 per cent. of the equity capital without control in the foreign entity and there is no other financial commitment other than by way of equity capital; or
- (ii) a foreign entity is under liquidation.

Explanation— For the purposes of this sub-regulation—

- (a) the APR shall be based on the audited financial statements of the foreign entity:

Provided that where the person resident in India does not have control in the foreign entity and the laws of the host country or host jurisdiction, as the case may be, do not provide for mandatory auditing of the books of accounts, the APR may be submitted based on unaudited financial statements certified as such by the statutory auditor of the Indian entity or by a chartered accountant where the statutory audit is not applicable;

- (b) in case more than one person resident in India have made ODI in the same foreign entity, the person holding the highest stake in the foreign entity shall be required to submit APR and in case of holdings being equal, APR may be filed jointly by such persons;

- (c) the person resident in India shall report the details regarding acquisition or setting up or winding up or transfer of a step down subsidiary or alteration in the shareholding pattern in the foreign entity during the reporting year in the APR.
- (5) An Indian entity which has made ODI shall submit an Annual Return on Foreign Liabilities and Assets within such time as may be decided by the Reserve Bank from time to time, to the Department of Statistics and Information Management, Reserve Bank of India.

Delay in reporting – According to regulation 11 following are the requirements to be complied with for delay in reporting:

- (1) A person resident in India who does not submit the evidence of investment within the time specified under sub-regulation (1) of regulation 9 or does not make any filing within the time specified under regulation 10, may make such submission or filing, as the case may be, along with Late Submission Fee within such period as may be advised, and at the rates and in the manner as may be directed by the Reserve Bank, from time to time:

Provided that such facility can be availed within a maximum period of three years from the due date of such submission or filing, as the case may be.

- (2) A person resident in India responsible for submitting the evidence or any filing relating to overseas investment in accordance with the Act or regulations made thereunder before the date of publication of these regulations in the Official Gazette and who has not made or does not make such submission or filing within the time specified thereunder, may make such submission or filing along with Late Submission Fee or make payment of Late Submission Fee where such submission or filing has been done, as the case may be, within such period as may be advised, and at the rates and in the manner as may be directed by the Reserve Bank, from time to time.

Provided that such facility can be availed within a maximum period of three years from the date of publication of these regulations in the Official Gazette.

Restriction on further financial commitment or transfer– Regulation 12 states of following restriction on financial commitment and transfer:

A person resident in India who has made a financial commitment in a foreign entity in accordance with the Act or rules or regulations made thereunder, shall not make any further financial commitment, whether fund-based or non-fund-based, directly or indirectly, towards such foreign entity or transfer such investment till any delay in reporting is regularised.

❖ **Export of goods and services (Section 7)**

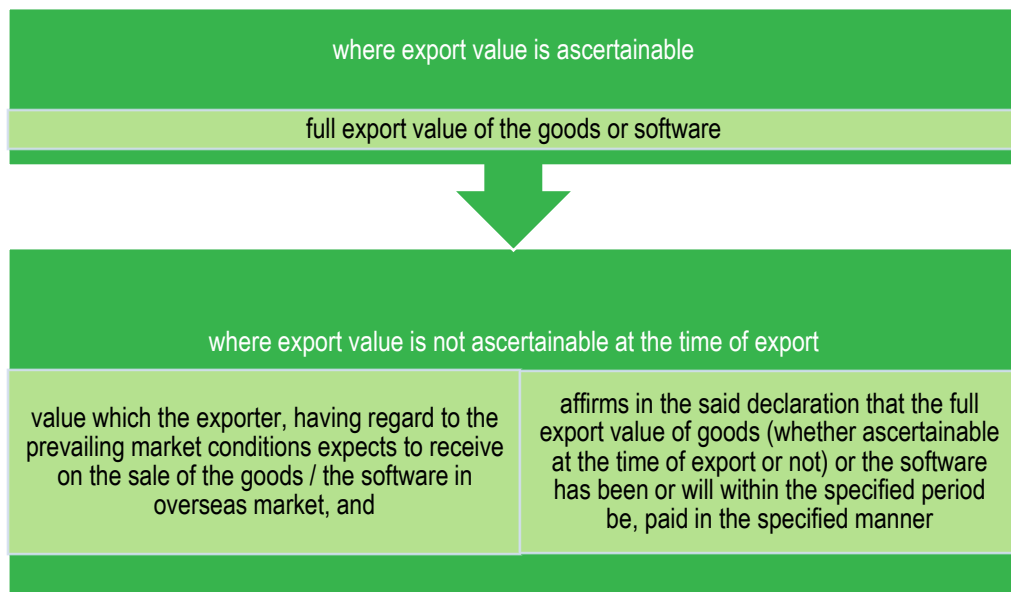
- (1) **Filing of declaration and other information:** Every exporter of goods shall-
 - (a) Furnish declaration to the Reserve Bank / to such other authority in such form and manner as may be specified. It will be containing true and correct material particulars, including the amount representing the full export value or, if the full export value of the goods is not ascertainable at the time of export, the value which the exporter, having

regard to the prevailing market conditions, expects to receive on the sale of the goods in a market outside India,

- (b) furnish to the Reserve Bank such other information as may be required by the Reserve Bank for the purpose of ensuring the realization of the export proceeds by such exporter.
- (2) **Direction to exporter to comply with requirements for ensuring export value of goods:** The Reserve Bank may, for the purpose of ensuring that the full export value of the goods or such reduced value of the goods as the Reserve Bank determines, having regard to the prevailing market conditions, is received without any delay, direct any exporter to comply with such requirements as it deems fit.
- (3) **Submission of declaration in relation to payment for such services:** Every exporter of services shall furnish to the Reserve Bank or to such other authorities a declaration in such form and in such manner as may be specified, containing the true and correct material particulars in relation to payment for such services.

Regulations:

1. **Short title and commencement:** These Regulations may be called the Foreign Exchange Management (Export of Goods and Services) Regulations, 2015 w.e.f. 12-1-2016.
2. **Definitions:- Some definitions:** In these Regulations, unless the context requires otherwise,
 - (i) **'export'** includes the taking or sending out of goods by land, sea or air, on consignment or by way of sale, lease, hire-purchase, or under any other arrangement by whatever name called, and in the case of software, also includes transmission through any electronic media;
 - (ii) **'export value'** in relation to export by way of lease or hire-purchase or under any other similar arrangement, includes the charges, by whatever name called, payable in respect of such lease or hire-purchase or any other similar arrangement;
 - (iii) **'form'** means form annexed to these Regulations;
 - (iv) **'software'** means any computer programme, database, drawing, design, audio/video signals, any information by whatever name called in or on any medium other than in or on any physical medium;
 - (v) **'specified authority'** means the person or the authority to whom the declaration as specified in Regulation 3 is to be furnished;
3. **Declaration of exports:** In case of exports taking place through Customs manual ports: every exporter of goods or software in physical or any other form, either directly or indirectly, to any place outside India, other than Nepal and Bhutan, shall furnish to the specified authority- a declaration in the forms set out in the Schedule with the support of evidence containing true and correct material particulars including the amount representing –



In respect of export of services to which none of the Forms specified in these Regulations apply: the exporter may export such services without furnishing any declaration, but shall be liable to realise the amount of foreign exchange which becomes due /accrues on account of such export, and to repatriate the same to India in accordance with the provisions of the Act, and these Regulations, as also other rules and regulations made under the Act.

Realization of export proceeds in respect of export of goods / software from third party should be duly declared by the exporter in the appropriate declaration form.

4. Exemptions: Export of goods / software may be made without furnishing the declaration in the following cases, namely:

- (a) trade samples of goods and publicity material supplied free of payment;
- (b) personal effects of travellers, whether accompanied or unaccompanied;
- (c) ship's stores, trans-shipment cargo and goods supplied under the orders of Central Government or of such officers as may be appointed by the Central Government in this behalf or of the military, naval or air force authorities in India for military, naval or air force requirements;
- (d) by way of gift of goods accompanied by a declaration by the exporter that they are not more than five lakh rupees in value;
- (e) aircrafts or aircraft engines and spare parts for overhauling and/or repairs abroad subject to their reimport into India after overhauling /repairs, within a period of six months from the date of their export;
- (ea) re-export of leased aircraft/helicopter and/or engines/auxiliary power units (APUs),

either completely or in partially knocked down condition re-possessed by overseas lessor and duly de-registered by the Directorate General of Civil Aviation (DGCA) on the request of Irrevocable Deregistration and Export Request Authorisation (IDERA) holder under 'Cape Town Convention' or any other termination or cancellation of the lease agreement between the lessor and lessee subject to permission by DGCA/Ministry of Civil Aviation for such export/s.

- (f) goods imported free of cost on re-export basis;
- (g) the following goods which are permitted by the Development Commissioner of the Special Economic Zones, Electronic Hardware Technology Parks, Software Technology Parks or Free Trade Zones to be re-exported, namely:
 - (1) imported goods found defective, for the purpose of their replacement by the foreign suppliers/collaborators;
 - (2) goods imported from foreign suppliers/collaborators on loan basis;
 - (3) goods imported from foreign suppliers/collaborators free of cost, found surplus after production operations.
- (ga) goods listed at items (1), (2) and (3) of clause (i) to be re-exported by units in Special Economic Zones, under intimation to the Development Commissioner of Special Economic Zones / concerned Assistant Commissioner or Deputy Commissioner of Customs
- (h) replacement goods exported free of charge in accordance with the provisions of Foreign Trade Policy in force, for the time being.
- (i) goods sent outside India for testing subject to re-import into India;
- (j) defective goods sent outside India for repair and re-import provided the goods are accompanied by a certificate from an authorised dealer in India that the export is for repair and re-import and that the export does not involve any transaction in foreign exchange.
- (k) exports permitted by the Reserve Bank, on application made to it, subject to the terms and conditions, if any, as stipulated in the permission.

5. **Indication of importer-exporter code number:** The importer-exporter code number (allotted by the Director General of Foreign Trade under Section 7 of the Foreign Trade (Development & Regulation) Act, 1992) shall be indicated on all copies of the declaration forms submitted by the exporter to the specified authority and shall be used in all correspondence of the exporter with the authorised dealer or the Reserve Bank, as the case may be.

6. **Authority to whom declaration is to be furnished and the manner of dealing with the declaration:**

Declaration in Form EDF	(i) It shall be submitted in duplicate to the Commissioner of Customs. (ii) After verification and authentication of the declaration form, the Commissioner of Customs shall forward the original declaration form/data to the nearest office of the Reserve Bank, and (iii) hand over the duplicate form to the exporter for being submitted to the authorised dealer.
Declaration in Form SOFTEX	(i) It shall be, in respect of export of computer software and audio/video/ television software, submitted in triplicate to the designated official of Ministry of Information Technology, Government of India at the Software Technology Parks of India (STPIs) or at the Free Trade Zones (FTZs) or Special Economic Zones (SEZs) in India. (ii) After certifying all three copies of the SOFTEX form, the designated official shall forward the original directly to the nearest office of the Reserve Bank and return the duplicate to the exporter. (iii) The triplicate shall be retained by the designated official for record.

Duplicate Declaration Forms to be retained with Authorised Dealers: On the realisation of the export proceeds, the duplicate copies of export declaration forms viz. EDF and SOFTEX shall be retained by the Authorised Dealers.

7. **Evidence in support of declaration:-** The Commissioner of Customs/ the postal authority/ the official of Department of Electronics, to whom the declaration form is submitted, may, in order to satisfy themselves of due compliance with Section 7 of the Act and these regulations, require such evidence in support of the declaration as may establish that –

- (a) the exporter is a person resident in India and has a place of business in India;
- (b) the destination stated on the declaration is the final place of the destination of the goods exported;
- (c) the value stated in the declaration represents –

- (i) the full export value of the goods or software; or
- (ii) where the full export value of the goods or software is not ascertainable at the time of export, the value which the exporter, having regard to the prevailing market conditions expects to receive on the sale of the goods in the overseas market.

Explanation—For the purpose of this regulation, 'final place of destination' means a place in a country in which the goods are ultimately imported and cleared through Customs of that country.

- 8. Manner of payment of export value of goods:** Unless otherwise authorised by the Reserve Bank, the amount representing the full export value of the goods exported shall be paid through an authorised dealer in the manner specified in the Foreign Exchange Management (Manner of Receipt and Payment) Regulations, 2000 as amended from time to time.

Explanation—For the purpose of this regulation, re-import into India, within the period specified for realisation of the export value, of the exported goods in respect of which a declaration was made under Regulation 3, shall be deemed to be realisation of full export value of such goods.

- 9. Period within which export value of goods/software/ services to be realised:-**

- (1) **In ordinary case:** The amount representing the full export value of goods / software/ services exported shall be realised and repatriated to India **within nine months or within such period** as may be specified by the Reserve Bank, in consultation with the Government, from time to time, from the date of export, provided.

However, **where the goods are exported to a warehouse established outside India** with the permission of the Reserve Bank, the amount representing the full export value of goods exported shall be paid to the authorised dealer as soon as it is realised and in any case within **fifteen months or within such period** as may be specified by the Reserve Bank, in consultation with the Government, from time to time from the date of shipment of goods;

Extension of period: Further the Reserve Bank, or subject to the directions issued by that Bank in this behalf, the authorised dealer may, for a sufficient and reasonable cause, extend the said period.

- (2) Where the export of goods / software / services has been made by Units in Special Economic Zones (SEZ) / Status Holder exporter / Export Oriented Units (EOUs) and units in Electronics Hardware Technology Parks (EHTPs), Software Technology Parks (STPs) and Bio-Technology Parks (BTPs) as defined in the Foreign Trade Policy in force, the amount representing the full export value of goods or software shall be realised and repatriated to India within nine months or within such period as may be specified by the Reserve Bank, in consultation with the Government, from time to time from the date of export.

Extension of period: Provided further that the Reserve Bank, or subject to the directions issued by the Bank in this behalf, the authorised dealer may, for a sufficient and reasonable cause shown, extend the said period.

The Reserve Bank may for reasonable and sufficient cause direct that the said exporter/s shall cease to be governed by above sub-regulation (2). Such a direction shall be given only when the unit has been given a reasonable opportunity to make a representation in the matter.

On such direction, the said exporter/s shall be governed by the provisions of sub-regulation (1), until directed otherwise by the Reserve Bank.

For the purpose of this regulation, the “date of export” in relation to the export of software in other than physical form, shall be deemed to be the date of invoice covering such export.

- 10. Submission of export documents:** The documents pertaining to export shall be submitted to the authorised dealer mentioned in the relevant export declaration form, within 21 days from the date of export, or from the date of certification of the SOFTEX form:

Provided that, subject to the directions issued by the Reserve Bank from time to time, the authorised dealer may accept the documents pertaining to export submitted after the expiry of the specified period of 21 days, for reasons beyond the control of the exporter.

- 11. Transfer of documents:** An authorised dealer may accept, for negotiation or collection, shipping documents including invoice and bill of exchange covering exports, from his constituent (not being a person who has signed the declaration in terms of Regulation 3):

Provided that before accepting such documents for negotiation or collection, the authorised dealer shall –

- (a) where the value declared in the declaration does not differ from the value shown in the documents being negotiated or sent for collection, or
- (b) where the value declared in the declaration is less than the value shown in the documents being negotiated or sent for collection, require the constituent concerned also to sign such declaration and thereupon such constituent shall be bound to comply with such requisition and such constituent signing the declaration shall be considered to be the exporter for the purposes of these Regulations to the extent of the full value shown in the documents being negotiated or sent for collection and shall be governed by these Regulations accordingly.

- 12. Payment for the Export:** In respect of export of any goods / software for which a declaration is required to be furnished, no person shall except with the permission of the Reserve Bank or, subject to the directions of the Reserve Bank, permission of an authorised dealer, do or refrain from doing anything or take or refrain from taking any action which has the effect of securing –

- (i) that the payment for the goods or software is made otherwise than in the specified manner; or
- (ii) that the payment is delayed beyond the period specified under these Regulations; or
- (iii) that the proceeds of sale of the goods or software exported do not represent the full export value of the goods or software subject to such deductions, if any, as may be allowed by the Reserve Bank or, subject to the directions of the Reserve Bank, by an authorised dealer;

Provided that no proceedings in respect of contravention of these provisions shall be instituted unless the specified period has expired and payment for the goods or software representing the full export value, or the value after deductions allowed under clause (iii), has not been made in the specified manner within the specified period.

- (iv) Export of services to which no Form specified in these Regulations apply, the exporter may export such services without furnishing any declaration, (i), (ii) & (iii) above shall apply.

13. Certain Exports requiring prior approval: Exports under trade agreement/rupee credit etc.

- (i) Export of goods under special arrangement between the Central Government and Government of a foreign state, or under rupee credits extended by the Central Government to Govt. of a foreign state shall be governed by the terms and conditions set out in the relative public notices issued by the Trade Control Authority in India and the instructions issued from time to time by the Reserve Bank.
- (ii) An export under the line of credit extended to a bank or a financial institution operating in a foreign state by the Exim Bank for financing exports from India, shall be governed by the terms and conditions advised by the Reserve Bank to the authorised dealers from time to time.

14. Delay in Receipt of Payment: Where in relation to goods or software export of which is required to be declared on the specified form and export of services, in respect of which no declaration forms has been made applicable, the specified period has expired and the payment therefor has not been made as aforesaid, the Reserve Bank may give to any person who has sold the goods or software or who is entitled to sell the goods or software or procure the sale thereof, such directions as appear to it to be expedient, for the purpose of securing,

- (a) the payment therefor if the goods or software has been sold and
- (b) the sale of goods and payment thereof, if goods or software has not been sold or reimport thereof into India as the circumstances permit, within such period as the Reserve Bank may specify in this behalf;

Provided that omission of the Reserve Bank to give directions shall not have the effect of absolving the person committing the contravention from the consequences thereof.

15. Advance payment against exports:

- (1) **Where an exporter receives advance payment (with or without interest), from a buyer / third party** named in the export declaration made by the exporter, outside India, the exporter shall be under an obligation to ensure that –
- (i) **the shipment of goods is made within one year** from the date of receipt of advance payment;
 - (ii) the rate of interest, if any, payable on the advance payment shall not exceed 100 basis points above the London Inter-Bank Offered Rate (LIBOR) or other applicable benchmark as may be directed by the Reserve Bank, as the case may be; and”
 - (iii) the documents covering the **shipment are routed through the authorised dealer** through whom the advance payment is received;

Provided that in the event of the exporter's inability to make the shipment, partly or fully, within one year from the date of receipt of advance payment, no remittance towards refund of unutilized portion of advance payment or towards payment of interest, shall be made after the expiry of the period of one year, without the prior approval of the Reserve Bank.

- (2) **Exemption:** Notwithstanding anything contained in clause (i) of sub-regulation (1), an exporter may receive advance payment where the export agreement itself duly provides for shipment of goods extending beyond the period of one year from the date of receipt of advance payment.

16. Issue of directions by Reserve Bank in certain cases:

- (1) In relation to the export of goods or software which is required to be declared, the Reserve Bank may, for the purpose of ensuring that the full export value of the goods or the value which the exporter having regard to the prevailing market conditions expects to receive on the sale of goods or software in the overseas market, is received in proper time and without delay, by general or special order, direct from time to time that in respect of export of goods or software to any destination or any class of export transactions or any class of goods or software or class of exporters, the exporter shall, prior to the export, comply with the conditions as may be specified in the order, namely;
- (a) that the payment of the goods or software is covered by an irrevocable letter of credit or by such other arrangement or document as may be indicated in the order;
 - (b) that any declaration to be furnished to the specified authority shall be submitted to the authorised dealer for its prior approval, which may, having regard to the circumstances, be given or withheld or may be given subject to

such conditions as may be specified by the Reserve Bank by directions issued from time to time.

- (c) that a copy of the declaration to be furnished to the specified authority shall be submitted to such authority or organisation as may be indicated in the order for certifying that the value of goods or software specified in the declaration represents the proper value thereof.
- (2) **Exception:** No direction under sub-regulation (1) shall be given by the Reserve Bank and no approval under clause (b) of that sub-regulation shall be withheld by the Authorised Dealer, unless the exporter has been given a reasonable opportunity to make a representation in the matter.

17. Project exports:

- (1) **Where an export of goods or services is proposed to be made on deferred payment terms or in execution of a turnkey project or a civil construction contract**, the exporter shall, before entering into any such export arrangement, submit the proposal for prior approval of the approving authority, which shall consider the proposal in accordance with the guidelines issued by the Reserve Bank of India from time to time.
- (2) **In case a guarantee is required to be given prior to post award approval**, the same may be issued by an authorized dealer bank/ a person resident in India being an exporting company, for performance of a project outside India, or for availing of credit facilities, whether fund-based or non-fund based, from a bank or a financial institution outside India in connection with the execution of such project, provided that the contract / Letter of Award stipulates such requirements. Explanation:

For the purpose of this Regulation, 'approving authority' means the EXIM Bank of India or the authorised dealer.

❖ Realisation and repatriation of foreign exchange [Section 8]

Foreign Exchange is a common resource and has a vital impact on interest rates and inflation. The funds belong to the individual but the equivalent foreign exchange belongs to the Government of India. Therefore all foreign exchange should be realized, repatriated and surrendered to the Reserve Bank through Authorised Persons. Permitted amounts can be held as foreign currency as per the guidelines issued from time to time.

Where any amount of foreign exchange is due or has accrued to any person resident in India, such person shall take all reasonable steps to realise and repatriate to India such foreign exchange within such period and in such manner as may be specified by the Reserve Bank.

Exemption from realisation and repatriation in certain cases [Section 9]

The provisions of sections 4 and 8 shall not apply to the following, namely:—

- (a) possession of foreign currency or foreign coins by any person up to such limit as the Reserve Bank may specify

- (b) foreign currency account held or operated by such person or class of persons and the limit up to which the Reserve Bank may specify
- (c) foreign exchange acquired or received before the 8th day of July, 1947 or any income arising or accruing thereon which is held outside India by any person in pursuance of a general or special permission granted by the Reserve Bank;
- (d) foreign exchange held by a person resident in India up to such limit as the Reserve Bank may specify, if such foreign exchange was acquired by way of gift or inheritance from a person referred to in clause (c), including any income arising there from;
- (e) foreign exchange acquired from employment, business, trade, vocation, services, honorarium, gifts, inheritance or any other legitimate means up to such limit as the Reserve Bank may specify; and
- (f) such other receipts in foreign exchange as the Reserve Bank may specify.



6 AUTHORISED PERSON [SECTION 10]

The term authorised person (AP) is defined under Section 2(c) of the Act to mean an authorised dealer, money changer, off-shore banking unit or any other person authorised to deal in foreign exchange or foreign securities.

Off Shore Banking Unit

An Off Shore Banking Unit means a branch of a bank in India, located in the Special Economic Zone. Although such an Off Shore Banking Unit may have a licence to operate as an Authorised Dealer, it shall not be regarded as an Authorised Dealer under Foreign Exchange Management Act, 1999.

An Off Shore Banking Unit shall NOT conduct any activity or undertake any transaction with residents in India. An Off Shore Banking Unit may undertake any transaction with any Authorised Dealer in India on Principal-to-Principal basis. Off Shore Banking Units are meant to facilitate units in Special Economic Zones and may undertake transactions in Foreign Exchange with a unit in the Special Economic Zone to the extent the latter is eligible to enter into or undertake such transactions.

Appointment of authorized person: The RBI has the power to appoint authorised person under Section 10 of the Act.

Appointment on application: Any person may be authorised by the Reserve Bank of India, on an application made to it in this behalf, **to deal in Foreign exchange or in foreign securities**. Such an authorised person may function as an authorised dealer, money changer or offshore banking unit or in any other manner as he deems fit.

Any such authorisation made by the RBI shall be in writing and shall be subject to the conditions laid down in the authorisation.

AP shall comply with the directions of the RBI : An authorized person must, in all his dealings in foreign exchange or foreign security, comply with such general or special directions or orders as the Reserve Bank may, from time to time, think fit to give. Also, except with the previous permission of the Reserve Bank, an authorized person may not engage in any transaction involving any foreign exchange or foreign security, which is not in conformity with the terms of his authorization.

AP may ask for declaration and information for carrying of any transaction on behalf of any person: Before commencement of any transactions in Foreign exchange on behalf of any person, an authorised person must insist that such person should make a declaration and give whatever information is required in order to satisfy him that the transaction will not involve and is not designed to contravene or evade the provisions of this Act or any Rule, Regulation, Notification, Direction, or order made under this Act.

In case of contravention/non-compliance of any requirement: If such person refuses to abide by such requirement or his compliance is not good enough, the authorised person shall refuse in writing to undertake the transaction. If the authorised person has reason to believe that any such contravention or evasion (as aforesaid) is contemplated by the other person, the authorised person shall report the matter to the Reserve Bank of India.

If any person, other than an authorized person, who has acquired or purchased foreign exchange for any purpose mentioned in the declaration made by him to authorized person

- Does not use it for such purpose or
- Does not surrender it to the authorized person within the specified period or
- Uses the foreign exchange so acquired or purchased for any other purpose for which purchase or acquisition of foreign exchange is not permissible under the provisions of the Act or the rules or regulations or direction or order made there under

Such person shall be deemed to have committed contravention of the provisions of the Act.

Revocation of authorisation: Any authorisation given by the Reserve Bank of India may be revoked by it, at any time, if it is satisfied that: -

1. It is in public interest so to do, or
2. The authorised person has failed to comply with the conditions laid down in the authorisation.
3. The authorised person has contravened any of the provisions of this Act or any Rule, Regulation, Notification, Direction, or order made under this Act.

An authorisation shall not be revoked on grounds mentioned in 2 and 3 above, unless the authorised person has been given a reasonable opportunity of making a representation in.

❖ Reserve Bank's powers to issue directions to authorised person [Section 11]

In order to secure strict compliance with the provisions of this Act and of any Rules, Regulations, Notifications, or directions, the Reserve Bank may direct the authorised persons with regard to :

1. Matters pertaining to
 - (i) Making of payment; or
 - (ii) The doing or desisting from doing of any act relating to Foreign Exchange or foreign security.
2. Furnishing such information, in such manner, as it deems fit.

Penalty for Contravention of Directions by an Authorised Person

Where any authorised person contravenes any direction given by the Reserve Bank under this Act or fails to file any return as directed by the Reserve Bank, the Reserve Bank may, after giving reasonable opportunity of being heard, impose on the authorised person a penalty which may extend to ten thousand rupees and in the case of continuing contravention with an additional penalty which may extend to two thousand rupees for every day during which such contravention continues.

Note: The Authorized person shall be given a reasonable opportunity of being heard before imposing penalty.

Power of Reserve Bank to inspect authorised person [Section 12]

It shall appear to the Reserve Bank that it is necessary and expedient to cause an inspection of the business of any Authorised person. There upon, it may at any time specially authorize any officer, in writing to inspect such business, such an inspection may be made for the following purpose:-

1. **Verification of the correctness** of any statement, information, or particulars furnished to the Reserve Bank.
2. **Obtaining any information or particulars**, which such authorised person, has failed to furnish, on being called upon to do so.
3. **Securing compliance** with the provisions of this Act or of any Rules, Regulations, Directions, or orders made under the Act.

Every authorized person is duty-bound

- (i) to **produce** such books, accounts and other documents in his custody or power to the officer making the inspection, and
- (ii) to **furnish** any statement relating to the affairs of such person, company or firm.

In the **case of company or firm** it shall be the duty of **every director, partner or other officer** of such company or firm.



7. CONTRAVENTIONS AND PENALTIES IN BRIEF

Section No.	Contravention	Quantum of Penalty
Section 11	By Authorised person any direction by RBI or failure to file any return as directed by RBI	➤ Upto ₹10,000. ➤ If continuing offence additional penalty upto ₹2,000 per day.
Section 13	Of any provision of the Act, or any rule, regulation, notification, direction or order or of any condition subject to which an authorization issued	➤ Upto three times, the sum involved, if it is quantifiable. ➤ If not quantifiable upto ₹2 lacs. ➤ If continuing offence, further penalty upto ₹5,000 per day after first day.
Section 13(1A) and 13(1C)	Acquisition of any foreign exchange, foreign security or immovable property, situated outside India, of the aggregate value exceeding the threshold prescribed under the proviso to sub-section (1) of section 37A	➤ Upto three times, the sum involved. ➤ confiscation of the value equivalent of foreign assets involved in contravention, situated in India. ➤ W.r.t contravention related to 13(1C), in addition to the penalty imposed above i.e. for 13(1A), Imprisonment upto 5 years and with a fine
Section 14	Failure to pay penalty as above – where demand is of an amount exceeding ₹1 crore. – in any other case	Civil imprisonment. ➤ Upto 3 years ➤ Upto 6 months.

Any Adjudicating Authority adjudging any contravention under section 13(1), may, if he thinks fit in addition to any penalty which he may impose for such contravention direct that any currency, security or any other money or property in respect of which the contravention has taken place shall be confiscated to the Central Government and further direct that the foreign exchange holdings, if any of the person committing the contraventions or any part thereof, shall be brought back into India or shall be retained outside India in accordance with directions made in this behalf.

Explanation: For the purposes of this sub-section, “property” in respect of which contravention has taken place, shall include:

- (a) deposits in a bank, where the said property is converted into such deposits;

- (b) Indian currency, where the said property is converted into that currency; and
- (c) any other property, which has resulted out of the conversion of that property.

❖ **Enforcement of the orders of Adjudicating Authority [Section 14]**

- (1) **In case of failure to make full payment of the penalty:** if any person fails to make full payment of the penalty imposed on him under section 13 within a period of ninety days from the date on which the notice for payment of such penalty is served on him, he shall be liable to civil imprisonment under this section.
- (2) **Order of arrest and detention in civil prison:** No order for the arrest and detention in civil prison of a defaulter shall be made unless the Adjudicating Authority has issued and served a notice upon the defaulter calling upon him to appear before him on the date specified in the notice and to show cause why he should not be committed to the civil prison, and unless the Adjudicating Authority, for reasons in writing, is satisfied:
 - (a) that the defaulter, with the object or effect of obstructing the recovery of penalty, has after the issue of notice by the Adjudicating Authority, dishonestly transferred concealed, or removed any part of his property, or
 - (b) that the defaulter has or has had since the issuing of notice by the Adjudicating Authority, the means to pay the arrears or some substantial part thereof and refuses or neglects or has refused or neglected to do the same.
- (3) **Issue of warrant for the arrest of the defaulter:** a warrant for the arrest of the defaulter may be issued by the Adjudicating Authority if the Adjudicating authority is satisfied, by affidavit or otherwise, that with the object or effect of delaying the execution of the certificate the defaulter is likely to abscond or leave the local limits of the jurisdiction of the Adjudicating Authority.
- (4) **In case of absence pursuant to the notice served:** Where appearance is not made pursuant to a notice issued and served, the Adjudicating Authority may issue a warrant for the arrest of the defaulter.
- (5) Every person arrested in pursuance of a warrant of arrest shall be brought before the Adjudicating Authority issuing the warrant as soon as practicable and in any event within twenty-four hours of his arrest (exclusive of the time required for the journey);

Provided that, if the defaulter pays the amount entered in the warrant of arrest as due and the costs of the arrest to the officer arresting him, such officer shall at once release him.

Default by HUF: Where the defaulter is a Hindu undivided family, the karta thereof shall be deemed to be the defaulter.

- (6) Where a defaulter appears before the Adjudicating Authority pursuant to a notice, the Adjudicating Authority shall give the defaulter an opportunity showing cause when he should not be committed to the civil prison.

- (7) **In case of pending of an inquiry:** the adjudicating Authority may, in his discretion, order the defaulter to be detained in the custody of such officer as the Adjudicating Authority may think fit or release him on his furnishing the security to the satisfaction of the Adjudicating Authority for his appearance as and when required.
- (8) **Upon the conclusion of the inquiry:** the Adjudicating Authority may make an order for the detention of the defaulter in the civil prison and shall in that event cause him to be arrested if he is not already under arrest:
- (9) **Upon satisfaction of arrears:** Provided that in order to give a defaulter an opportunity of satisfying the arrears, the Adjudicating Authority may, before making the order of detention, leave the defaulter in the custody of the officer arresting him or of any other officer for a specified period not exceeding fifteen days, or release him on his furnishing security to the satisfaction of the adjudicating authority for his appearance at the expiration of the specified period if the arrears are not satisfied.
- (10) **Order of release:** When the Adjudicating Authority does not make an order of detention, he shall, if the defaulter is under arrest, direct his release.
- (11) Every person detained in the civil prison in execution of the certificate may be so detained:
 - (a) where the certificate is for a demand of an amount exceeding rupees one crore, up to three years, and
 - (b) in any other case, up to six months:

Provided that he shall be released from such detention on the amount mentioned in the warrant for his detention being paid to the officer-in-charge of the civil prison.
- (12) **Defaulter liable for payment of arrears:** A defaulter released from detention under this section shall not, merely by reason of his release, be discharged from his liability for the arrears, but he shall not be liable to be arrested under the certificate in execution of which he was detained in the civil prison.
- (13) **Execution of detention order:** A detention order may be executed at any place in India in the manner provided for the execution of warrant of arrest under the Code of Criminal Procedure, 1973.

❖ **Power to recover arrears of penalty [Section 14A]**

- (1) **An officer of Enforcement to recover any arrears of penalty:** The Adjudicating Authority may, by order in writing, authorise an officer of Enforcement (not below the rank of Assistant Director) to recover any arrears of penalty from any person who fails to make full payment of penalty imposed on him under section 13 within the period of ninety days from the date on which the notice for payment of such penalty is served on him.
- (2) **Powers:** The officer of Enforcement, shall exercise all the like powers which are conferred on the income-tax authority in relation to recovery of tax under the Income-tax Act, 1961 and the

procedure laid down under the Second Schedule to the said Act shall mutatis mutandis apply in relation to recovery of arrears of penalty under this Act.



8. COMPOUNDING OF OFFENCES

Compounding Authority: Persons authorized by Central Government under section 15 i.e. classes of officers of the Enforcement Directorate and classes of officers of the RBI can act as Compounding Authority.

According to section 15:

- (1) **Period of compounding of an offence:** Any contravention under section 13 may, on an application made by the person committing such contravention, be compounded within **one hundred and eighty days from the date of receipt of application** by the Director of Enforcement or such other officers of the Directorate of Enforcement and Officers of the Reserve Bank as may be authorised in this behalf by the Central Government in such manner as prescribed under the Foreign Exchange (Compounding Proceedings) Rules, 2000.
- (2) **In case of compounding, no proceeding may be initiated:** Where a contravention has been compounded, no proceeding or further proceeding, as the case may be, shall be initiated or continued, as the case may be, against the person committing such contravention under that section, in respect of the contravention so compounded.

Case Law: In *Sterlite Industries (India) Ltd. v. Special Director of Enforcement, Mumbai*, it laid down that once a contravention has been compounded under section 15(1), no proceeding or further proceeding, as case may be, shall be initiated or continued, against person committing contravention.



9. ADJUDICATION AND APPEAL

Time limits

Section No.	Obligation	Time Limit
Section 14	Full penalty to be paid	Within 90 days from the date on which notice for payment of penalty is served.
Section 15	Compounding of Contravention under section 13	Within 180 days of receipt of application by Directorate of Enforcement or RBI
Section 16	Complaint under section 16(1) to be dealt by Adjudicated Authority	Within 1 year of receipt of complaint.
Section 17	Appeal to Special Director (Appeals)	Within 45 days from receipt of order.

Section 19	Appeal to Appellate Tribunal	Within 45 days from receipt of order.
Section 19(5)	Appeal to be dealt with by Appellate Tribunal	Will try to dispose off the appeal within 180 days from receipt of appeal.
Section 35	Appeal to High Court	Within 60 days of communication of order or decision.

❖ Appointment of Adjudicating Authority

For the purpose of adjudication under section 13, the Central Government may, by an order published in the Official Gazette, appoint as many officers of the Central Government as it may think fit, as the Adjudicating Authorities for holding an inquiry in the manner prescribed after giving the person alleged to have committed contravention under section 13, against whom a complaint has been made under sub-section (3) (hereinafter in this section referred to as the said person) a reasonable opportunity of being heard for the purpose of imposing any penalty:

Provided that where the Adjudicating Authority is of opinion that the said person is likely to abscond or is likely to evade in any manner, the payment of penalty, if levied, it may direct the said person to furnish a bond or guarantee for such amount and subject to such conditions as it may deem fit. [Section 16 (1)]

Adjudicating Authority shall hold an enquiry upon a complaint in writing made by any officer authorized by a general or special order by the Central Government [Section 16(3)]

Every Adjudicating Authority shall deal with the complaint as expeditiously as possible and endeavour shall be made to dispose of the complaint finally within one year from the date of receipt of the complaint:

Provided that where the complaint cannot be disposed of within the said period, the Adjudicating Authority shall record periodically the reasons in writing for not disposing of the complaint within the said period. [Section 16 (6)]

❖ Appeal to Special Director (Appeals)

- (1) The Central Government shall, by notification, **appoint one or more Special Directors (Appeals)** to hear appeals against the orders of the Adjudicating Authorities under this section and shall also specify in the said notification the matter and places in relation to which the Special Director (Appeals) may exercise jurisdiction. [Section 17(1)]
- (2) Any **person aggrieved** by an order made by the Adjudicating Authority, being an Assistant Director of Enforcement or a Deputy Director of Enforcement, **may prefer an appeal** of the Special Director (Appeals). [Section 17(2)]
- (3) Every appeal shall be **filed within forty-five days** from the date on which the copy of the order made by the Adjudicating Authority is received by the aggrieved person. [Section 17(3)]

- (4) The Special Director (Appeals) may **entertain an appeal after the expiry of the said period** of forty-five days, if he is satisfied that there was **sufficient cause** for not filing it within that period.

❖ **Appeal to Appellate Tribunal [Section 18]**

The Appellate Tribunal constituted under section 12(1) of the Smugglers and Foreign Exchange Manipulators (Forfeiture of Property) Act, 1976, (SAFEMA) shall be the Appellate Tribunal for the purposes of this Act and the said Appellate Tribunal shall exercise the jurisdiction, powers and authority conferred on it by or under this Act [Section 18].

The Central Government or any person aggrieved by an order made by an Adjudicating Authority, other than those referred to in sub-section (1) of section 17, or the Special Director (Appeals), may prefer an appeal to the Appellate Tribunal [Section 19(1)]. Every appeal shall be filed within a period of forty-five days from the date on which a copy of the order made by the Adjudicating Authority or the Special Director (Appeals) is received by the aggrieved person or by the Central Government. [Section 19(2)]. Where any appeal could not be disposed of within the said period of one hundred and eighty days, the Appellate Tribunal shall record its reasons in writing for not disposing of the appeal within the said period.[Section 19(5)]

❖ **Appeal to High Court (Section 35)**

Any person aggrieved by any decision or order of the Appellate Tribunal may file an appeal to the High Court within sixty days from the date of communication of the decision or order of the Appellate Tribunal on any question of law arising out of such order:

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

Explanation: In this section “High Court” means:

- (a) the High Court within the jurisdiction of which the aggrieved party ordinarily resides or carries on business or personally works for gain; and
- (b) where the Central Government is the aggrieved party, the High Court within the jurisdiction of which the respondent, or in a case where there are more than one respondent, any of the respondents, ordinarily resides or carries on business or personally works for gain.



10. DIRECTORATE OF ENFORCEMENT

❖ **Directorate of Enforcement (Section 36)**

- (1) The Central Government shall establish a Directorate of Enforcement with a Director and such other officers or class of officers as it thinks fit, who shall be called officers of Enforcement, for the purposes of this Act.

- (2) The Central Government may authorise the Director of Enforcement or an Additional Director of Enforcement or a Special Director of Enforcement or a Deputy Director of Enforcement to appoint officers of Enforcement below the rank of an Assistant Director of Enforcement.
- (3) Subject to such conditions and limitations as the Central Government may impose, an officer of Enforcement may exercise the powers and discharge the duties conferred or imposed on him under this Act.

Power of search and seizure: The Director of Enforcement and other officers of Enforcement, not below the rank of an Assistant Director, shall take up for investigation the contravention referred to in section 13. [Section 37(1)]

❖ Empowering other officers (Section 38)

- (1) The Central Government may, by order and subject to such conditions and limitations as it thinks fit to impose, authorise any officer of customs or any central excise officer or any police officer or any other officer of the Central Government or a State Government to exercise such of the powers and discharge such of the duties of the Director of Enforcement or any other officer of Enforcement under this Act as may be stated in the order.
- (2) The officers referred to in sub-section (1) shall exercise the like powers which are conferred on the income-tax authorities under the Income-tax Act, 1961, subject to such conditions and limitations as the Central Government may impose.

11. MISCELLANEOUS

❖ Presentation as to documents in certain cases [Section 39]

Where any document:

- (i) is produced or furnished by any person or has been seized from the custody or control of any person, in either case, under this Act or under any other law; or
- (ii) has been received from any place outside India (duly authenticated by such authority or person and in such manner as may be prescribed) in the course of investigation of any contravention under this Act alleged to have been committed by any person, such document is tendered in any proceeding under this Act in evidence against him, or against him and any other person who is proceeded against jointly with him, the court or the Adjudicating Authority, as the case may be, shall:
 - (a) presume, unless the contrary is proved, that the signature and every other part of such document which purports to be in the handwriting of any particular person or which the court may reasonably assume to have been signed by, or to be in the handwriting of any particular person, is in that person's handwriting and in the case of a document executed or attested, that it was executed or attested by the person by whom it purports to have been so executed or attested;

- (b) admit the document in evidence notwithstanding that it is not duly stamped, if such document is otherwise admissible in evidence;
- (c) in a case falling under clause (i), also presume, unless the contrary is proved, the truth of the contents of such document.

❖ **Suspension of operation of this Act [Section 40]**

- (1) If the Central Government is satisfied that circumstances have arisen rendering it necessary that any permission granted or restriction imposed by this Act should cease to be granted or imposed, or if it considers necessary or expending so to do in public interest, the Central Government may, by notification, suspend or relax to such extent either indefinitely or for such period as may be notified, the operation of all or any of the provisions of this Act.
- (2) Where the operation of any provision of this Act has under sub-section (1) been suspended or relaxed indefinitely, such suspension or relaxation may, at any time while this Act remains in force, be removed by the Central Government by notification.
- (3) Every notification issued under this section shall be laid, as soon as may be after it issued, before each House of Parliament, while it is in session, for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the notification or both Houses agree that the notification should not be issued, the notification shall thereafter have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that notification.

❖ **Power of Central Government to give directions [Section 41]**

For the purposes of this Act, the Central Government may, from time to time, give to the Reserve bank such general or special directions as it thinks fit, and the Reserve bank shall, in the discharge of its functions under this Act, comply with any such directions.

❖ **Contravention by companies [Section 42]**

- (1) **Where a person committing a contravention any of the provisions of this Act or of any rule, direction or order made thereunder is a company**, every person who, at the time the contravention was committed, was in charge of, and was responsible to, the company for the conduct of the business of the company as well as the company, shall be deemed to be guilty of the contravention and shall be liable to be proceeded against and punished accordingly [Sub-section (1)].

Provided that nothing contained in this sub-section shall render any such person liable to punishment if he proves that the contravention took place without his knowledge or that he exercised due diligence to prevent such contravention.

- (2) **Where contravention of any of the provisions of this Act or of any rule, direction or order made thereunder has been committed by a company** and it is proved that the contravention has taken place with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer of the company shall also be deemed to be guilty of the contravention and shall be liable to be proceeded against and punished accordingly.

Explanation: For the purpose of this Section—

- (i) “Company” means anybody corporate and includes a firm or other association of individuals; and
- (ii) “Director” in relation to a firm, means a partner in the firm.

❖ **Death or insolvency in certain cases [Section 43]**

Any right, obligation, liability, proceedings or appeal arising in relation to the provision of section 13 shall not abate by reason of death or insolvency of the person liable under that section and upon such death or insolvency such rights and obligations shall devolve on the legal representative of such person or the official receiver or the official assignee, as the case may be:

Provided that a legal representative of the deceased shall be liable only to the extent of the inheritance or estate of the deceased.

❖ **Bar Legal proceedings [Section 44]**

No suit, prosecution or other legal proceeding shall lie against the Central Government or the Reserve Bank or any officer of that Government or of the Reserve Bank or other person exercising any power or discharging any functions or performing any duties under this Act, for anything in good faith done or intended to be done under this Act or any rule, regulation, notification, direction or order made thereunder.

Students may note that though they are not expected to know the details of all the Rules/Regulations/Clarifications/Notifications issued by various authorities from time to time. However, they should familiarise with such Notifications and other significant rules/regulations having a bearing on such provisions of the Act and which are covered as part of the Study Material and Revision Test Papers published from time to time.

TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. *In September, 2020, Mr. Purshottam Saha visited Atlanta as well as Athens and thereafter, London and Berlin on a month-long business trip, for which he withdrew foreign exchange to the extent of US\$ 50,000 from his banker State Bank of India, New Delhi branch. In December, 2020 he further, withdrew US\$ 50,000 from SBI and remitted the same to his son Raviyansh Saha who was studying in Toronto, Canada. In the first week of January, 2021, he sent his ailing mother Mrs. Savita Saha for a specialised treatment along with his wife Mrs. Rashmi Saha to Seattle where his younger brother Pranav Saha, holder of Green Card, is residing. For the purpose of his mother's treatment and to help Pranav Saha to meet increased expenses, he requested his banker SBI to remit US\$ 75,000 to Pranav Saha's account maintained with Citibank, Seattle. In February, 2021, Mr. Purshottam Saha's daughter Devanshi Saha got engaged and she opted for a 'destination marriage' to be held in August, 2021 in Zurich, Switzerland. While on a trip to Dubai in the last week of March, 2021, he again withdrew US\$ 35,000 to be used by him and Devanshi Saha for meeting various trip expenses including shopping in Dubai. Later, the event manager gave an estimate of US\$ 2,50,000 for the wedding of Devanshi Saha at Zurich, Switzerland. Which option do you think is the correct one in the light of applicable provisions of Foreign Exchange Management Act, 1999 including obtaining of prior approval, if any, from Reserve Bank of India since Mr. Purshottam Saha withdrew foreign exchange on various occasions from his banker State Bank of India.*
 - (a) *In respect of withdrawal of foreign exchange on various occasions from his banker State Bank of India and remitting the same outside India during the financial year 2020-21, Mr. Purshottam Saha is not required to obtain any prior approval.*
 - (b) *In respect of withdrawal of US\$ 35,000 in the last week of March, 2021, for a trip to Dubai, Mr. Purshottam Saha must have obtained prior approval of Reserve Bank of India since the maximum amount of foreign exchange that can be withdrawn in a financial year is US\$ 1,75,000.*
 - (c) *After withdrawing US\$ 1,00,000, Mr. Purshottam Saha must have obtained prior approval of Reserve Bank of India for the remaining remittances made during the financial year 2020-21, otherwise SBI would not have permitted further withdrawals.*
 - (d) *After withdrawing US\$ 50,000, Mr. Purshottam Saha must have obtained prior approval of Reserve Bank of India for the remaining remittances made during the financial year 2020-21, otherwise SBI would not have permitted further withdrawals.*
2. *M/s. Kedhar Sports Academy, a private coaching club, provides coaching for cricket, football and other similar sports. It coaches sports aspirants pan India. It also conducts various sports events and campaigns, across the country. In 2022, to mark the 25th year of its operation, a*

cricket tournament (akin to the format of T-20) is being organized by M/s. Kedhar Sports Academy in Lancashire, England, in the first half of April. The prize money for the 'winning team' is fixed at USD 40,000 whereas in case of 'runner-up', it is pegged at USD 11,000. You are required to choose the correct option from the four given below which signifies the steps to be taken by M/s. Kedhar Sports Academy for remittance of the prize money of USD 51,000 (i.e. USD 40,000+USD 11,000) to England keeping in view the relevant provisions of Foreign Exchange Management Act, 1999:

- (a) For remittance of the prize money of USD 51,000, M/s Kedhar Sports Academy is required to obtain prior permission from the Ministry of Human Resource Development (Department of Youth Affairs and Sports).
 - (b) For remittance of the prize money of USD 51,000, M/s Kedhar Sports Academy is required to obtain prior permission from the Reserve Bank of India.
 - (c) For remittance of the prize money of USD 51,000, M/s Kedhar Sports Academy is not required to obtain any prior permission from any authority, whatsoever, and it can proceed to make the remittance.
 - (d) For remittance of the prize money of USD 51,000, M/s Kedhar Sports Academy is required to obtain prior permission from the Ministry of Finance (Department of Economic Affairs).
3. Akash Ceramics Limited, an Indian company, holds a commercial plot in Chennai which it intends to sell. M/s. Super Seller, a real estate broker with its Head Office in the USA, has been appointed by Akash Ceramics Limited to find some suitable buyers for the said commercial plot in Chennai which is situated at a prime location. M/s. Super Seller identifies Glory Estate Inc., based out of USA, as the potential buyer. It is to be noted that Glory Estate Inc. is controlled from India and hence, is a 'Person Resident in India' under the applicable provisions of Foreign Exchange Management Act, 1999. A deal is finalised and Glory Estate Inc. agrees to purchase the commercial plot for USD 600,000 (assuming 1 USD = ₹70). According to the agreement, Akash Ceramics Limited is required to pay commission @ 7% of the sale proceeds to M/s. Super Seller for arranging the sale of commercial plot to Glory Estate Inc. and commission is to be remitted in USD to the Head Office of M/s. Super Seller located in USA. Considering the relevant provisions of Foreign Exchange Management Act, 1999, which statement out of the four given below is correct (ignoring TDS implications arising under the Income-tax Act, 1961):
- (a) There is no requirement of obtaining prior permission of Reserve Bank of India (RBI) for remittance of commission upto USD 25,000 by Akash Ceramics Limited to M/s. Super Seller but for the balance commission of USD 17,000, prior permission of RBI is required to be obtained.
 - (b) There is no requirement of obtaining prior permission of Reserve Bank of India (RBI) for remittance of commission upto USD 30,000 by Akash Ceramics Limited to M/s. Super

Seller but for the balance commission of USD 12,000, prior permission of RBI is required to be obtained.

- (c) *There is no requirement of obtaining prior permission of Reserve Bank of India (RBI) for remittance of entire commission of USD 42,000 by Akash Ceramics Limited to M/s. Super Seller.*
 - (d) *It is mandatory to obtain prior permission of Reserve Bank of India (RBI) for remittance of entire commission of USD 42,000 by Akash Ceramics Limited to M/s. Super Seller.*
4. *Mr. Raman, a non-resident Indian, has a Systematic Investment Plan (SIP) with a prominent Indian mutual fund. Due to some impending financial difficulties, he requested his elder brother Mr. Raghav, a resident Indian currently working as Manager in a multi-national company at Mumbai, to make payment of a few subsequent instalments of SIP on his behalf. Which option, do you think, correctly signifies whether Mr. Raghav is permitted to undertake such transaction of paying a few instalments of SIP on behalf of his nonresident brother considering the applicable provisions of the Foreign Exchange Management Act, 1999:*
- (a) *Mr. Raghav is not permitted to undertake such transaction of paying a few instalments of SIP on behalf of his non-resident brother since it amounts to payment for the credit of a nonresident person.*
 - (b) *Mr. Raghav is permitted to undertake such transaction of paying a few instalments of SIP on behalf of his non-resident brother since Mr. Raman is his real brother.*
 - (c) *Mr. Raghav is permitted to undertake such transaction of paying a few instalments of SIP on behalf of his non-resident brother only if his employer permits.*
 - (d) *Mr. Raghav is permitted to undertake such transaction of paying a few instalments of SIP on behalf of his non-resident brother only if he obtains prior permission of Reserve Bank of India.*
5. *Mohita Periodicals and Mags Publications Limited, having registered office in Chennai, has obtained consultancy services from an entity based in France for setting up a software programme to strengthen various aspects relating to publications. The consideration for such consultancy services is required to be paid in foreign currency. The compliance officer of Mohita Periodicals and Mags Publications Limited, Mrs. Ritika requires your advice regarding the foreign exchange that can be remitted for the purpose of obtaining consultancy services from abroad without prior approval of Reserve Bank of India. Out of the following four options, choose the one which correctly portrays the amount of foreign exchange remittable for the given purpose after considering the provisions of the Foreign Exchange Management Act, 1999 and regulations made thereunder:*

- (a) *Permissible amount of foreign exchange that can be remitted by Mohita Periodicals and Mags Publications Limited for obtaining consultancy services from an entity based in France without prior approval of RBI is US\$ 50,000,000.*
 - (b) *Permissible amount of foreign exchange that can be remitted by Mohita Periodicals and Mags Publications Limited for obtaining consultancy services from an entity based in France without prior approval of RBI is US\$ 10,000,000.*
 - (c) *Permissible amount of foreign exchange that can be remitted by Mohita Periodicals and Mags Publications Limited for obtaining consultancy services from an entity based in France without prior approval of RBI is US\$ 5,000,000.*
 - (d) *Permissible amount of foreign exchange that can be remitted by Mohita Periodicals and Mags Publications Limited for obtaining consultancy services from an entity based in France without prior approval of RBI is US\$ 1,000,000.*
6. *After five years of stay in USA, Mr. Umesh came to India at his paternal place in New Delhi on October 25, 2019, for the purpose of conducting business with his two younger brothers Rajesh and Somesh and contributed a sum of ` 10,00,000 as his capital. Simultaneously, Mr. Umesh also started a proprietary business of selling artistic brassware, jewelry, etc. procured directly from the manufacturers based at Moradabad. Within a period of two months after his arrival from USA, Mr. Umesh established a branch of his proprietary business at Minnesota, USA. You are required choose the appropriate option with respect to residential status of Mr. Umesh and his branch for the financial year 2020-21 after considering the applicable provisions of the Foreign Exchange Management Act, 1999:*
- (a) *For the financial year 2020-21, Mr. Umesh and his branch established at Minnesota, USA, are both persons resident outside India.*
 - (b) *For the financial year 2020-21, Mr. Umesh is a resident in India but his branch established at Minnesota, USA, is a person resident outside India.*
 - (c) *For the financial year 2020-21, Mr. Umesh and his branch established at Minnesota, USA, are both persons resident in India.*
 - (d) *For the financial year 2020-21, Mr. Umesh is a person resident outside India but his branch established at Minnesota, USA, is a person resident in India.*

Descriptive Questions

1. *'Printex 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 Branch in Dubai which is controlled by the Headquarters in Pune. What would be the residential status under the FEMA, 1999 of printer units in Pune and that of Dubai branch?*

2. Mr. Sane, an Indian National desires to obtain Foreign Exchange for the following purposes:
 - (i) Remittance of US Dollar 50,000 out of winnings on a lottery ticket.
 - (ii) US Dollar 100,000 for sending a cultural troupe on a tour of U.S.A.Advise him whether he can get Foreign Exchange and if so, under what conditions?
3. State which kind of approval is required for the following transactions under the Foreign Exchange Management Act, 1999:
 - (i) X, a Film Star, wants to perform along with associates in New York on the occasion of Diwali for Indians residing at New York. Foreign Exchange drawal to the extent of US dollars 20,000 is required for this purpose.
 - (ii) R wants to get his heart surgery done at United Kingdom. Up to what limit Foreign Exchange can be drawn by him and what are the approvals required?
4. Referring to the provisions of the Foreign Exchange Management Act, 1999, examine whether V, an exporter is bound to make declaration of a gift of Jewellery valued at ` 20,000 exported from India to United Kingdom.
5. Referring to the provisions of the Foreign Exchange Management Act, 1999, state the kind of approval required for the following transactions:
 - (i) M requires U.S. \$ 5,000 for remittance towards hiring charges of transponders.
 - (ii) P requires U.S. \$ 2,000 for payment related to call back services of telephones.
6. Suresh resided in India during the Financial Year 2013-14. He left India on 15th July, 2014 for Switzerland for pursuing higher studies in Biotechnology for 2 years. What would be his residential status under the Foreign Exchange Management Act, 1999 during the Financial Years 2014-15 and 2015-16?

Mr. Suresh requires every year USD 25,000 towards tuition fees and USD 30,000 for incidental and stay expenses for studying abroad. Is it possible for Mr. Suresh to get the required Foreign Exchange and, if so, under what conditions?
7.
 - (i) Mr. P has won a big lottery and wants to remit US Dollar 20,000 out of his winnings to his son who is in USA. Advise whether such remittance is possible under the Foreign Exchange Management Act, 1999.
 - (ii) Mr. Z is unwell and would like to have a kidney transplant done in USA. He would like to know the formalities required and the amount that can be drawn as foreign exchange for the medical treatment abroad.
8. Mr. Rohan, an Indian Resident individual desires to obtain Foreign Exchange for the following purposes:

- (A) US\$ 120,000 for studies abroad on the basis of estimates given by the foreign university.
 (B) Gift Remittance amounting US\$ 10,000.

Advise him whether he can get Foreign Exchange and if so, under what condition(s)?

ANSWERS

Answer to Multiple Choice Questions

1.	a	2.	c	3.	d	4.	a	5.	d
6.	c								

Answer to Descriptive Questions

- Printex Computer being a Singapore based company would be person resident outside India [(Section 2(w)]. Section 2 (u) defines 'person' under clause (viii) thereof, as person would include any agency, office or branch owned or controlled by such person. The term such person appears to refer to a person who is included in clause (i) to (vi). Accordingly, Printex unit in Pune, being a branch of a company would be a 'person'.

Section 2(v) defines a person resident in India. Under clause (iii) thereof person resident in India would include an office, branch or agency in India owned or controlled by a person resident outside India. Printex unit in Pune is owned or controlled by a person resident outside India, and hence it, would be a 'person resident in India.'

However, Dubai Branch though not owned, is controlled by the Printer unit in Pune which is a person resident in India. Hence, the Dubai Branch is a person resident in India.

- Under provisions of section 5 of the Foreign Exchange Management Act, 1999 certain Rules have been made for drawal of Foreign Exchange for Current Account transactions. As per these Rules, Foreign Exchange for some of the Current Account transactions is prohibited. As regards some other Current Account transactions, Foreign Exchange can be drawn with prior permission of the Central Government while in case of some Current Account transactions, prior permission of Reserve Bank of India is required.
 - In respect of item No.(i), i.e., remittance out of lottery winnings, such remittance is prohibited and the same is included in First Schedule to the Foreign Exchange Management (Current Account Transactions) Rules, 2000. Hence, Mr. Sane can not withdraw Foreign Exchange for this purpose.
 - Foreign Exchange for meeting expenses of cultural tour can be withdrawn by any person after obtaining permission from Government of India, Ministry of Human Resources Development, (Department of Education and Culture) as prescribed in Second Schedule to the Foreign Exchange Management (Current Account Transactions) Rules, 2000.

Hence, in respect of item (ii), Mr. Sane can withdraw the Foreign Exchange after obtaining such permission.

In all the cases, where remittance of Foreign Exchange is allowed, either by general or specific permission, the remitter has to obtain the Foreign Exchange from an Authorised Person as defined in Section 2(c) read with section 10 of the Foreign Exchange Management Act, 1999.

3. Approval to the following transactions under FEMA, 1999:

- (i) Foreign Exchange draws for cultural tours require prior permission/approval of the Ministry of Human Resources Development (Department of Education and Culture) irrespective of the amount of foreign exchange required. Therefore, in the given case X, the Film Star is required to seek permission of the said Ministry of the Government of India.
- (ii) Individuals can avail of foreign exchange facility within the limit of USD 2,50,000 only. Any additional remittance in excess of the said limit for the expenses requires an approval from RBI. However in connection with medical treatment abroad, no approval of the Reserve Bank of India is required. Therefore, R can draw foreign exchange up to amount estimated by a medical institute offering treatment.

- 4.** In accordance with provisions of the FEMA, 1999 as contained in section 7 read with section 8, an exporter shall make appropriate declaration of the value of the goods being exported and he is also required to repatriate the foreign exchange due to India in respect of such exports to India in the manner within the time as may be prescribed. Under section 8, the exporter is under an obligation to realise and repatriate to India such foreign. However, if there is an delay in the receipt of export, it will not be a violation which shall be punishable. Section 8 applies to a resident who shall take all the reasonable steps, depending upon the individual case.

There are certain categories of export for which declaration need not be made. These are given under the Regulation 4 of the Foreign Exchange Management (Export of Goods & Services) Regulations, 2015. According to the regulation, export of goods by way of gift shall be accompanied by a declaration / undertaking by the exporter confirming that they are not more than five lakh rupees in value. Taking into consideration the above, since the value of gift of jewellery to V's friend in the United Kingdom is less than ` 5 lac in value, declaration (as per the format specified in the regulations) is not required to be furnished by the exporter to the specified authority.

- 5.** Under section 5 of the Foreign Exchange Management Act, 1999, and Rules relating thereto, some current account transactions require prior approval of the Central Government, some others require the prior approval of the Reserve Bank of India, some are freely permitted transactions and some others are prohibited transactions. Accordingly,
- (i) It is a current account transaction, where M is required to take approval of the Central Government for drawal of foreign exchange for remittance of hire charges of transponders.

(ii) Withdrawal of foreign exchange for payment related to call back services of telephone is a prohibited transaction. Hence, Mr. P cannot obtain US \$ 2,000 for the said purpose.

6. **Residential Status:** According to section 2(v) of the Foreign Exchange Management Act, 1999, 'Person resident in India' means a person residing in India for more than 182 days during the course of preceding financial year [Section 2(v)(i)]. However, it does not include a person who has gone out of India or who stays outside India for employment outside India or for any other purpose in such circumstances as would indicate his intention to stay outside India for an uncertain period.

Generally, a student goes out of India for a certain period. In this case, Mr. Suresh who resided in India during the financial year 2013-14 left on 15.7.2014 for Switzerland for pursuing higher studies in Biotechnology for 2 years, he will be resident as he has gone to stay outside India for a 'certain period' RBI has however clarified in its AP circular no. 45 dated 8th December 2003, that students will be considered as non-residents. This is because usually students start working there to take care of their stay and cost of studies.

Mr. Suresh will be treated as person resident in India for Financial Year 2014-2015 till 16th July 2014 and from 17th July 2014, he will be considered as person resident outside India.

However, during the Financial Year 2015-2016, Mr. Suresh will be considered as person resident outside India as he left India on 15th July 2014.

Foreign Exchange for studies abroad: According to Para I of Schedule III to Foreign Exchange Management (Current Account Transactions), Amendment Rule, 2015 dated 26th May, 2015, individuals can avail of foreign exchange facility for the studies abroad within the limit of USD 2,50,000 only. Any additional remittance in excess of the said limit shall require prior approval of the RBI. Further proviso to Para I of Schedule III states that individual may be allowed remittances (without seeking prior approval of the RBI) exceeding USD 2,50,000 based on the estimate received from the institution abroad. In this case the foreign exchange required is only USD 55,000 per academic year and hence approval of RBI is not required.

7. **Remittance of Foreign Exchange (Section 5 of the Foreign Exchange Management Act, 1999):** According to section 5 of the FEMA, 1999, any person may sell or draw foreign exchange to or from an authorized person if such a sale or drawal is a current account transaction. Provided that Central Government may, in public interest and in consultation with the reserve bank, impose such reasonable restrictions for current account transactions as may be prescribed.

As per the rules, drawal of foreign exchange for current account transactions are categorized under three headings-

1. Transactions for which drawal of foreign exchange is prohibited,
2. Transactions which need prior approval of appropriate government of India for drawal of foreign exchange, and

3. Transactions which require RBI's prior approval for drawl of foreign exchange.
- (i) Mr. P wanted to remit US Dollar 20,000 out of his lottery winnings to his son residing in USA. Such remittance is prohibited and the same is included in the Foreign Exchange Management (Current Account Transactions) Rules, 2000.
Hence Mr. P cannot withdraw foreign exchange for this purpose.
 - (ii) "Remittance of foreign exchange for medical treatment abroad" requires prior permission or approval of RBI where the individual requires withdrawal of foreign exchange exceeding USD 250,000. The Schedule also prescribes that for the purpose of expenses in connection with medical treatment, the individual may avail of exchange facility for an amount in excess of the limit prescribed under the Liberalized Remittance Scheme, if so required by a medical institute offering treatment.

Therefore, Mr. Z can draw foreign exchange up to the USD 250,000 and no prior permission/ approval of RBI will be required. For amount exceeding the above limit, authorised dealers may release foreign exchange based on the estimate from the doctor in India or hospital or doctor abroad.

- 8 (A) **Remittance of Foreign Exchange for studies abroad:** Foreign exchange may be released for studies abroad up to a limit of US \$ 250,000 for the studies abroad without any permission from the RBI. Above this limit, RBI's prior approval is required. Further proviso to Para I of Schedule III states that individual may be allowed remittances exceeding USD 250,000 based on the estimate received from the institution abroad. In this case since US \$ 120,000 is the drawal of foreign exchange, so permission of the RBI is not required.
- (B) **Gift remittance exceeding US \$ 10,000:** Under the provisions of Section 5 of FEMA 1999, certain Rules have been made for drawal of foreign exchange for current account transactions. Gift remittance is a current account transaction. Gift remittance exceeding US \$ 250,000 can be made after obtaining prior approval of the RBI. In the present case, since the amount to be gifted by an individual, Mr. Rohan is USD 10,000, there is no need for any permission from the RBI.

[illegible]

CHAPTER

2

THE FOREIGN CONTRIBUTION (REGULATION) ACT, 2010



LEARNING OUTCOMES

By the end of this Chapter, you will be able to-

- ❑ Know and appreciate significant terminologies used in the Act
- ❑ Determine how the law regulates the acceptance and utilization of foreign contribution or Foreign Hospitality
- ❑ Identify the restrictions on acceptance and utilisation of foreign contribution or Foreign Hospitality
- ❑ Explain the procedure for the registration of persons to be regulated in this Act
- ❑ Elucidate how persons regulated by the Act are required to manage the financial aspects of Foreign Contribution
- ❑ Recognise the Adjudicating Authority, the provisions related to appeal and revision, and offences and penalties on contravention of the compliances



1. INTRODUCTION

The Preamble to the Indian constitution defines India as a 'Sovereign' country, meaning India has its own supreme law and is not a dominion or province of any other nation. Moreover, India is independent of any kind of external intervention in its domestic operations. Therefore, no other country or international body can infringe on India's sovereignty. One of the threats to the sovereignty of India could be through transfer of funds from foreign sources as Foreign Contribution for any activities detrimental to the national interest.

The Foreign Contribution (Regulation) Act, 2010, together with the Foreign Contribution (Regulation) Rules, 2011 and other notification and orders, issued thereunder from time to time regulates the flow of foreign contributions into India and ensures that such contributions do not adversely affect national security. First enacted in 1976, it was amended in 2010 when new measures were adopted to regulate foreign contributions with effect from 1st May, 2011. The Foreign Contribution (Regulation) Act, 2010 was again amended through the Foreign Contribution (Regulation) Amendment Act, 2020 with effect from 28th September, 2020. The FCRA is administered by Ministry of Home Affairs.

Amendments made by the 2020 Amendment Act – Following were the highlights of the Foreign Contribution (Regulation) Amendment Act, 2020:

- ◆ No Foreign contribution can be accepted by a public servant, Judge, Government servant or employee of any corporation or any other body controlled or owned by the Government [section 3(1)(c) of FCRA, 2010]
- ◆ Amendment Act completely prohibits transfer of foreign contribution to any other person - [section 7 of FCRA, 2010].
- ◆ Defraying of foreign contribution towards administrative expenses reduced to 20% from 50% of contribution received – [section 8(1) of FCRA, 2010].
- ◆ Central Government may restrict or prohibit a person granted “prior permission” from either utilising the unutilized foreign contribution or receive remaining portion of foreign contribution if it has reason to believe that provisions of the Act have been contravened – [proviso to section 11(2) of FCRA, 2010].
- ◆ Every person who makes an application for “prior permission” or “registration” to open an “FCRA Account” as specified in section 17 – [section 12 (1A) of FCRA, 2010].
- ◆ Aadhaar number of all functionaries Resident in India and copy of Passport or OCI card in case of foreigner mandatory for application of prior permission or registration under FCRA or renewal thereof – [section 12A of FCRA, 2010].

- ◆ Suspension of certificate under consideration for cancellation extended for a further period, not exceeding one hundred and eighty days, beyond the initial suspension period of one hundred and eighty days – [section 13 of FCRA, 2010].
- ◆ Provision made for Surrender of Certificate of Registration under FCRA and the management of foreign contribution and asset to vest with such authority as specified – [section 14A of FCRA, 2010].
- ◆ All foreign contributions to be received in the designated 'FCRA Account', namely State Bank of India, New Delhi Main Branch (SBI-NDMB). May open another “FCRA account” in any of the scheduled bank for the purpose of keeping or utilising the foreign contribution received in the SBI “FCRA Account”. May also open one or more accounts in one or more scheduled banks to which funds may be transferred for utilising any foreign contribution, subject to the condition that no local contributions shall be deposited in this account– [section 17 of FCRA, 2010].

Vide Notification G.S.R. 695(E) [F. NO. II/21022/23(12)/2020-FCRA-III], dated 10-11-2020, in exercise of the powers conferred by section 48 of the Foreign Contribution (Regulation) Act, 2010, the Central Government hereby makes the following rules further to amend the Foreign Contribution (Regulation) Rules, 2011, through the enforcement of the Foreign Contribution (Regulation) (Amendment) Rules, 2020 w.r.e.f 29.04.2011.

Structure of the Act

The Foreign Contribution (Regulation) Act, 2010, (FCRA, 2010) comprises of nine chapters with 54 sections.

Chapter No.	Chapter Name
Chapter I	Preliminary (Section 1- 2)
Chapter II	Regulation of Foreign Contribution and Foreign Hospitality (Section 3 -10)
Chapter III	Registration (Section 11- 16)
Chapter IV	Accounts, Intimation, Audit and Disposal of Assets, etc. (Section 17- 22)
Chapter V	Inspection, Search and Seizure (section 23-27)
Chapter VI	Adjudication (Section 28-29)
Chapter VII	Appeal and Revision (Section 31- 32)
Chapter VIII	Offences and Penalties (Section 33- 41)
Chapter IX	Miscellaneous (Section 42- 54)

Extent, Application and Commencement of FCRA (Section 1)

As per Section 1(2) of FCRA, 2010, the provisions of the Act shall apply to:

- Whole of India
- Citizens of India outside India; and
- Associate Branches or subsidiaries, outside India, of companies or bodies corporate, registered or incorporated in India.

In line with the stated provision, the Act is applicable to any citizen of India whether he is in India or outside India. However, the Act is not applicable to a foreigner while outside India.

Note: An Indian passport holder would continue to be treated as a local source, irrespective of his stay outside India and outside the purview of FCRA whereas a Person of Indian Origin holding a foreign passport will be considered a foreign source and FCRA shall apply.

As per section 1(3) of the Act, the Central Government has appointed the 1st May, 2011 as the date on which the provisions of the said Act came into force.

**2. IMPORTANT DEFINITIONS (SECTION 2)**

In this Act, unless the context otherwise requires,—

"FCRA Account" [Section 2(1)(f)]

FCRA Account means the FCRA Account referred to in section 17 of the Act.

"Foreign Company" [Section 2(1)(g)]

Foreign Company means any company or association or body of individuals incorporated outside India and includes :—

- a foreign company within the meaning of section 591 of the Companies Act, 1956 (Section 379 of the Companies Act, 2013)
- Company which is a subsidiary of a foreign company;
- the registered office or principal place of business of a foreign company;
- a multi-national corporation.

Explanation— A corporation incorporated in a foreign country or territory shall be deemed to be a multi-national corporation if such corporation,—

- has a subsidiary or a branch or a place of business in two or more countries or territories; or
- carries on business, or otherwise operates, in two or more countries or territories;

Illustration 1: A Company is incorporated in India under the Companies Act, 2013 and has operations in 2 or more countries. Would it be treated as a MNC under FCRA, 2010?

Answer. No

Foreign Source [Section 2(1)(j)]

Foreign Source includes,—

- (i) the Government of any foreign country or territory and any agency of such Government;
- (ii) any international agency, not being the United Nations or any of its specialized agencies, the World Bank, International Monetary Fund or such other agency as the Central Government may, by notification, specify in this behalf;
- (iii) a foreign company;
- (iv) a corporation, not being a foreign company, incorporated in a foreign country or territory;
- (v) a multi-national corporation referred to in Section 2(g) sub-clause (iv) of FCRA, 2010;
- (vi) a company within the meaning of the Companies Act, 1956 (presently, the Companies Act, 2013) and more than one-half of the nominal value of its share capital is held, either singly or in the aggregate, by one or more of the following, namely:-
 - A. the Government of a foreign country or territory;
 - B. the citizens of a foreign country or territory;
 - C. corporations incorporated in a foreign country or territory;
 - D. trusts, societies or other associations of individuals (whether incorporated or not), formed or registered in a foreign country or territory;
 - E. Foreign company;

Provided that where the nominal value of share capital is within the limits specified for foreign investment under the Foreign Exchange Management Act, 1999, or the rules or regulations made there under, then, notwithstanding the nominal value of share capital of a company being more than one-half of such value at the time of making the contribution, such company shall not be a foreign source

[Clarity provided in the FAQs issued under FCRA by the Ministry of Home Affairs - I. Introduction to the Foreign Contribution (Regulation) Act, 2010 (FCRA, 2010)]

- (vii) a trade union in any foreign country or territory, whether or not registered in such foreign country or territory;
- (viii) a foreign trust or a foreign foundation, by whatever name called, or such trust or foundation mainly financed by a foreign country or territory;
- (ix) a society, club or other association or individuals formed or registered outside India;
- (x) a citizen of a foreign country;”

DEFINITION OF FOREIGN SOURCE

Government of any foreign country / agency of such government

International agency

foreign company

Corporation incorporated in a foreign country/territory

MNC

Company

Trade Union

Foreign trust/foundation

Society, club, association/individuals registered outside India

Citizen of foreign country

A few bodies/ organisations of the United Nations, World Bank (including the International Monetary Fund (IMF) and some other International agencies or multilateral organisations are exempted from this definition, and are not treated as foreign source. Hence, the funds received from them are not considered as foreign contribution.

Foreign Contribution [Section 2(1)(h)]

Foreign Contribution means the donation, delivery or transfer made by any **foreign source**,—

(i) **of any article**,

Exception: An article given to a person as a gift for his personal use, if the market value, in India, of such article, on the date of such gift, is not more than Rs. 1,00,000/- as per Rule 6A of the Foreign Contribution (Regulation) Rules, 2011 as amended by Foreign Contribution (Regulation) (Second Amendment) Rules, 2019 notified vide G.S.R. 659 (E) dated 16th September, 2019.

(ii) **any currency**, whether Indian or foreign;

(iii) **of any security** as defined in the Securities Contracts (Regulation) Act, 1956 and includes any foreign security as defined in the Foreign Exchange Management Act, 1999;

Explanations	Nature of contribution	Whether Foreign contribution or not
Explanation 1	A donation, delivery or transfer of any article, currency or foreign security by any person who has received it from any foreign source, either directly or through one or more persons	Shall also be deemed to be foreign contribution within the meaning of this clause

Explanation 2	• The interest accrued on the foreign contribution deposited in any bank referred to in section 17(1), or • any other income derived from the foreign contribution or interest thereon	
Explanation 3	• Any amount received, by any person from any foreign source in India, by way of fee (including fees charged by an educational institution in India from foreign student), or • towards cost in lieu of goods or services rendered by such person in the ordinary course of his business, trade or commerce whether within India or outside India, or • any contribution received from an agent of a foreign source towards such fee or cost	Shall be excluded from the definition of foreign contribution within the meaning of this clause;

Illustration: Whether earnings from foreign client(s) by a person in lieu of goods sold or a service rendered by it is treated as foreign contribution?

Answer: No. As per the above explanation 3, foreign contribution excludes earnings from foreign client(s) by a person in lieu of goods sold or services rendered by it as this is a transaction of commercial nature.

Illustration: Can foreign contribution be received in rupees?

Answer. Yes, any donation, delivery or transfer received from a 'foreign source' whether in rupees or in foreign currency is construed as 'foreign contribution' under FCRA, 2010. Such transactions even in rupees terms are considered as foreign contribution.

Illustration: Will interest or any other income earned from foreign contribution be considered foreign contribution?

Answer: Yes. It will become part of Foreign contribution (see Explanation 2)

Illustration: Whether donation given by Non-Resident Indians (NRIs) is treated as 'foreign contribution'?

Answer: Foreign Contribution is defined under section 2(1)(h) to mean the donation, delivery or transfer made by any foreign source. Section 2(1)(i) only speaks about citizen of a foreign country while inclusively defining Foreign Source. Therefore, contributions made by a citizen of India living

in another country (i.e., Non-Resident Indian), from his personal savings, through the normal banking channels, is not to be treated as foreign contribution. However, while accepting any donations from such NRI, it is advisable to obtain his passport details to ascertain that he/she is actually an Indian citizen.

Illustration: Whether 100% subsidiary of foreign company in IT sector can give donation to trust who doesn't have registration under FCRA?

Answer: Yes, it can. As per proviso of Section 2(1)(j)(vi) since the investment is within limits of FEMA, hence though it may be a 100% subsidiary of a foreign company it will not be considered a foreign source.

Illustration: Whether an Individual of Indian Origin who has acquired foreign nationality is treated as foreign source?

Answer: Yes. All citizens of a foreign country are treated as "Foreign Source", including Persons of Indian Origin holding foreign passport.

Person [Section 2(1)(m)]

Person includes:

- (i) an individual;
- (ii) a Hindu undivided family;
- (iii) an association;

a company registered under section 25 of the Companies Act, 1956 (now Section 8 of Companies Act, 2013).

Foreign Hospitality [Section 2(1)(i)]

Foreign Hospitality means any offer, not being a purely casual one, made in cash or kind by a foreign source for providing a person with the costs of travel to any foreign country or territory or with free boarding, lodging, transport or medical treatment.

Political party [Section 2(1)(n)]

Political party means—

- (i) an association or body of individual citizens of India—
 - (A) to be registered with the Election Commission of India as a political party under section 29A of the Representation of the People Act, 1951, or
 - (B) which has set up candidates for election to any Legislature, but is not so registered or deemed to be registered under the Election Symbols (Reservation and Allotment) Order, 1968;
- (ii) a political party mentioned in column 2 of Table 1 and Table 2 to the notification of the Election Commission of India No. 56/J&K/02, dated the 8th August, 2002, as in force for the time being;

Relative [Section 2(1)(r)]

"Relative" has the meaning assigned to it in section 2(41) of the Companies Act, 1956 (Now section 2(77) of the Companies Act, 2013)

Any words and expressions used in FCRA, 2010 but not defined in the said Act shall carry the meaning as defined in the Representation of the People Act, 1950 or the Representation of the People Act, 1951 or the Foreign Exchange Management Act, 1999. [Section 2(2)]



3. REGULATION OF FOREIGN CONTRIBUTION AND FOREIGN HOSPITALITY

Chapter II of the Act deals with the regulation of foreign contribution and foreign hospitality. It covers sections 3 to 10 of the Act. The chapter broadly focuses on certain prohibitions on acceptance of Foreign Contribution and restrictions on acceptance of Foreign Hospitality by certain classes of persons.

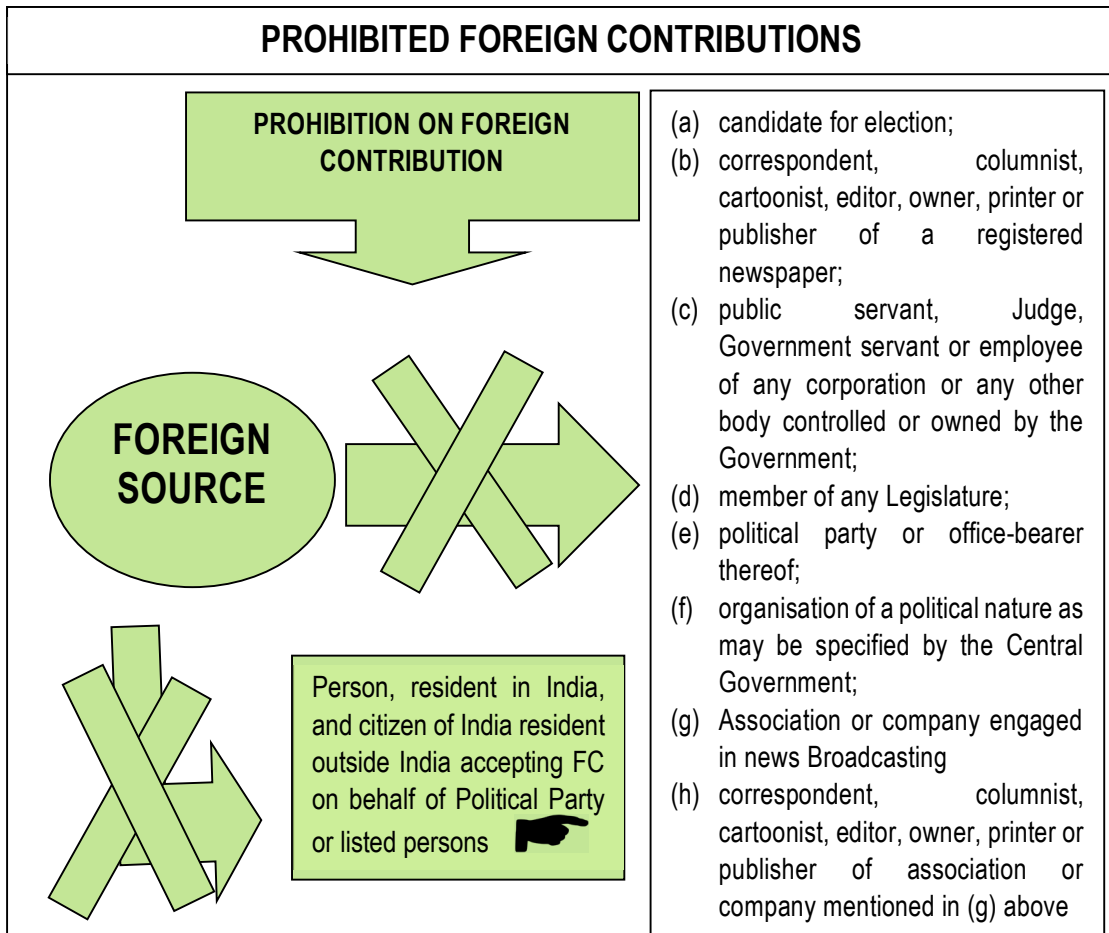
(I) Prohibition to accept foreign contribution (Section 3)

- (1) No foreign contribution shall be accepted by any:
 - (a) candidate for election;
 - (b) correspondent, columnist, cartoonist, editor, owner, printer or publisher of a registered newspaper;
 - (c) public servant, Judge, Government servant or employee of any corporation or any other body controlled or owned by the Government;
 - (d) member of any Legislature;
 - (e) political party or office-bearer thereof;
 - (f) organisation of a political nature as may be specified under section 5(1) by the Central Government;
 - (g) association or company engaged in the production or broadcast of audio news or audio visual news or current affairs programmes through any electronic mode, or any other electronic form as defined in the Information Technology Act, 2000 or any other mode of mass communication;
 - (h) correspondent or columnist, cartoonist, editor, owner of the association or company referred to in clause (g).

Explanation 1. - For the purpose of clause (c), "public servant" means a public servant as defined in section 21 of the Indian Penal Code (45 of 1860).

Explanation 2. - In clause (c) and section 6, the expression "corporation" means a corporation owned or controlled by the Government and includes a Government company as defined in clause (45) of section 2 of the Companies Act, 2013 (18 of 2013).

- (2) The prohibition mentioned in Section 3(1) above deals with direct acceptance of Foreign Contribution. Section 3(2) of the Act also prohibits indirect acceptance of foreign contribution by / through the following persons:
 - (a) **Person, resident in India, and citizen of India resident outside India** - shall not accept any foreign contribution, or acquire or agree to acquire any currency from a foreign source, on behalf of any political party, or any person referred to in (1) above, or both.
 - (b) **Person, resident in India**- shall not deliver any currency, whether Indian or foreign, which has been accepted from any foreign source, to any person if he knows or has reasonable cause to believe that such other person intends, or is likely, to deliver such currency to any political party or any person referred to in (1) above, or both.
 - (c) **Citizen of India resident outside India**- shall not deliver any currency, whether Indian or foreign, which has been accepted from any foreign source, to—
 - (i) any political party or any person referred to in (1) above, or both; or
 - (ii) any other person, if he knows or has reasonable cause to believe that such other person intends, or is likely, to deliver such currency to a political party or to any person referred to (1) above, or both.
- (3) Section 9 of FCRA, 2010 empowers the Central Government to prohibit or regulate acceptance of Foreign Contribution or Foreign Hospitality by persons not specified in (1) above. Any person receiving any currency, whether Indian or foreign, from a foreign source on behalf of any person or class of persons referred to in section 9 shall not deliver such currency—
 - (a) to any person other than a person for which it was received, or
 - (b) to any other person, if he knows or has reasonable cause to believe that such other person intends, or is likely, to deliver such currency to a person other than the person for which such currency was received.



Procedure to notify an organisation of a political nature (Section 5)

Certain organisations may not be registered as a political party, but their activities and the ideologies propagated by them may be such as to be closely aligned with that of a registered political party. This section empowers the Central Government to identify these organizations and notify them as organisation of a political nature. Thereafter, the provisions of the Act will apply to these organisations as if they are an organisation of a political nature mentioned in section 3 (1) (f).

The Central Government may be satisfied that an organisation is of a political nature, having regard to the activities of the organisation or the ideology propagated by the organisation or the programme of the organisation or the association of the organisations with the activities of any political party.

Central Government has clarified the guidelines specifying the ground or grounds on which an organisation shall be specified as an organisation of a political nature in Rule 3 of the Foreign Contribution (Regulation) Rules, 2011.

(II) Exceptions i.e. situations where section 3 shall not apply (Section 4)

Nothing contained in section 3 shall apply to the acceptance, by any person specified in that section, of any foreign contribution where such contribution is accepted by him, —

- (a) **by way of salary, wages or other remuneration** due to him or to any group of persons working under him, from any foreign source or by way of payment in the ordinary course of business transacted in India by such foreign source; or
- (b) **by way of payment**, in the course of international trade or commerce, or in the ordinary course of business transacted by him outside India; or
- (c) **as an agent of a foreign source** in relation to any transaction made by such foreign source with the Central Government or State Government; or
- (d) **by way of a gift or presentation** made to him as a member of any Indian delegation, provided that such gift or present was accepted in accordance with the rules made by the Central Government with regard to the acceptance or retention of such gift or presentation; or
- (e) **from his relative**; or

Note: Any person receiving foreign contribution in excess of ten lakh rupees or equivalent thereto in a financial year from any of his relatives shall inform the Central Government regarding the details of the foreign contribution received by him in electronic form in Form FC-1 within three months from the date of receipt of such contribution.

- (f) **by way of remittance received**, in the ordinary course of business through any official channel, post office, or any authorised person in foreign exchange under the Foreign Exchange Management Act, 1999 ; or
- (g) **by way of any scholarship, stipend or any payment** of like nature:

In case any foreign contribution is received by any person specified under section 3, for any of the purposes other than those specified above, such contribution shall be deemed to have been accepted in contravention of the provisions of section 3.

The point to be noted is that where foreign contribution is accepted for the above purposes or in any of the above circumstances, such contribution is exempted even if received by a person prohibited under section 3.

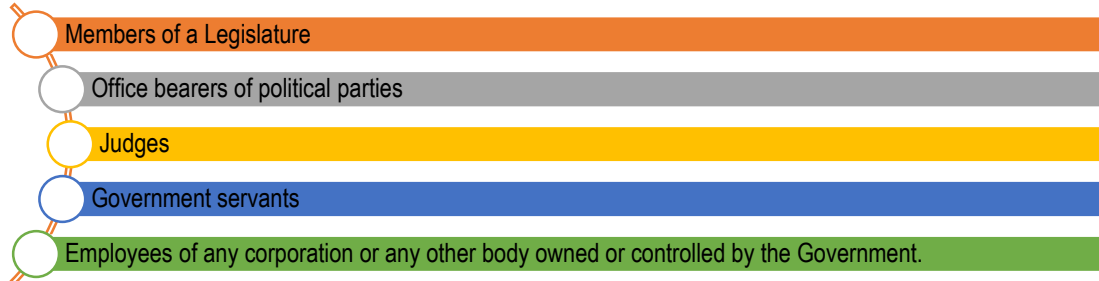
Illustration: Whether foreign remittances received from a relative are to be treated as foreign contribution as per FCRA, 2010?

Answer: No. As per Section 4(e) of FCRA, 2010 and FCRR, 2011, amounts received from relatives are NOT treated as foreign contribution even if received by a person prohibited to receive foreign contribution under section 3. However, in terms of Rule 6 of FCRR, 2011, any person receiving foreign contribution in excess of ten lakh rupees or equivalent thereto in a financial year from any of

his relatives shall inform the Central Government by uploading details electronically online in Form FC-1 within three months from the date of receipt of such contribution.

(III) Restriction on acceptance of foreign hospitality (Section 6)

As per Section 6 of the Act, following categories of persons require prior permission of the Central Government before accepting Foreign Hospitality, while visiting any country or territory outside India,:-



Exception: It shall not be necessary to obtain any such permission for an **emergent**¹ medical aid needed on account of sudden illness contracted during a visit outside India.

Intimation to CG in case of availing Foreign hospitality: But, where such foreign hospitality (in connection with an emergent medical aid) has been received, the person receiving such hospitality shall give an intimation to the Central Government as to the receipt of such hospitality within one month from the date of receipt of such hospitality, and the source from which, and the manner in which, such hospitality was received.

As per Rule 7 of the Foreign Contribution (Regulation), Rules 2011, foreign hospitality may be received by specified categories of persons in the following manner:

- (1) Any person belonging to any of the categories specified in section 6 who wishes to avail of foreign hospitality shall apply to the Central Government in electronic form to the Central Government in prescribed Form for prior permission to accept such foreign hospitality.
- (2) Every application for acceptance of foreign hospitality shall be accompanied by an invitation letter from the host or the host country, as the case may be, and administrative clearance of the Ministry or department concerned in case of visits sponsored by a Ministry or department of the Government.
- (3) The application for grant of permission to accept foreign hospitality must reach the appropriate authority ordinarily two weeks before the proposed date of onward journey.
- (4) In case of emergent medical aid needed on account of sudden illness during a visit abroad, the acceptance of foreign hospitality shall be required to be intimated to the Central Government within One month of such receipt giving full details including the source,

¹ Emergent means "in the process of coming into being or becoming prominent." In all probability, the intention of the legislature was to indicate an "emergency" which is something that arises unexpectedly.

approximate value in Indian Rupees, and the purpose for which and the manner in which it was utilised.

However, no such intimation is required if the value of such hospitality in emergent medical aid is upto one lakh rupees or equivalent thereto.

(IV) Prohibition to transfer foreign contribution to other person (Section 7)

No person who -

- (a) is registered and granted a certificate or has obtained prior permission under this Act; and
- (b) receives any foreign contribution,

shall transfer such foreign contribution to any other person.

Earlier, foreign contribution accepted with the permission of the Central Government could be transferred to any other person who was registered under FCRA, 2010 or had obtained prior permission or sought prior approval from Central Government to a person who had neither registration nor prior permission. It can be seen that the legislature has placed a blanket prohibition on transfer of foreign contribution received by any person to any other person. The intention is to prevent recipients of foreign contribution acting as mere conduits or facilitating agents for obtaining foreign contributions.

(V) Restriction to utilize foreign contribution for administrative purpose (Section 8)

- (1) Every person, who is registered and granted a certificate or given prior permission under this Act and receives any foreign contribution, shall—
- (a) **utilise such contribution for the purposes for which the contribution has been received:**

Any foreign contribution or any income arising out of it shall not be used for speculative business;

The Central Government shall, by rules, specify the activities or business which shall be construed as speculative business for the purpose of this section;

Speculative activities have been defined in Rule 4 of FCR, Rule 2011 as under:-

- (i) any activity or investment that has an element of risk of appreciation or depreciation of the original investment, linked to market forces, including investment in mutual funds or in shares;
- (ii) participation in any scheme that promises high returns like investment in chits or land or similar assets not directly linked to the declared aims and objectives of the organization or association.

Note: A debt-based secure investment shall not be treated as speculative investment.

- (b) not defray² as far as possible such sum, not exceeding **twenty per cent** of such contribution, received in a financial year, to meet administrative expenses:

Administrative expenses exceeding **twenty per cent** of such contribution may be defrayed with prior approval of the Central Government.

The Central Government may prescribe the elements which shall be included in the administrative expenses and the manner in which the administrative expenses shall be calculated.

Amounts that constitute Administrative Expenses

- (i) salaries, wages, travel expenses or any remuneration realised by the Members of the Executive Committee or Governing Council of the person;
- (ii) all expenses towards hiring of personnel for management of the activities of the person and salaries, wages or any kind of remuneration paid, including cost of travel, to such personnel;
- (iii) all expenses related to consumables like electricity and water charges, telephone charges, postal charges, repairs to premise(s) from where the organisation or Association is functioning, stationery and printing charges transport and travel charges by the Members of the Executive Committee or Governing Council and expenditure on office equipment;
- (iv) cost of accounting for and administering funds;
- (v) expenses towards running and maintenance of vehicles;
- (vi) cost of writing and filing reports;
- (vii) legal and professional charges; and
- (viii) rent of premises, repairs to premises and expenses on other utilities:

Amounts not to be counted as administrative expenses:

1. Expenditure incurred on salaries or remuneration of personnel engaged in training or for collection or analysis of field data of an association primarily engaged in research or training;
2. Expenses incurred directly in furtherance of the stated objectives of the welfare oriented organisation such as salaries to doctors of hospital, salaries to teachers of school etc.;

(VI) Power of Central Government to prohibit receipt of foreign contribution, etc., in certain cases (Section 9)

The Central Government shall be satisfied that the acceptance of foreign contribution by any person or class of persons, as the case may be, or the acceptance of foreign hospitality by any person, is likely to affect prejudicially—

- (i) the sovereignty and integrity of India; or

² Defray means “to provide for payment of”

³ Regulation - 5, Foreign Contribution (Regulation) Rules, 2011

- (ii) public interest; or
- (iii) freedom or fairness of election to any Legislature; or
- (iv) friendly relations with any foreign State; or
- (v) harmony between religious, racial, social, linguistic or regional groups, castes or communities.

Then, the Central Government may—

- (a) prohibit any person or organisation (not specified in section 3), from accepting any foreign contribution;
- (b) require any person or class of persons, (not specified in section 6), to obtain prior permission of the Central Government before accepting any foreign hospitality;
- (c) require any person or class of persons (not specified in section 11), to furnish intimation as to the amount of any foreign contribution received by such person or class of persons as the case may be, and the source from which and the manner in which such contribution was received and the purpose for which and the manner in which such foreign contribution was utilised;
- (d) require any person or class of persons specified in that Section 11(1) to obtain prior permission of the Central Government before accepting any foreign contribution;
- (e) require any person or class of persons, (not specified in section 6), to furnish intimation, as to the receipt of any foreign hospitality, the source from which and the manner in which such hospitality was received.

(VII) Power to prohibit payment of currency received in contravention of the Act (Section 10)

Where the Central Government is satisfied, after making such inquiry, that any person has in his custody or control any-

- article or
- currency or
- security,

whether Indian or foreign, which has been accepted by such person in contravention of any of the provisions of this Act, it may, by order in writing prohibit such person from-paying,

- delivering,
- transferring
- or otherwise dealing with,
- such article or currency or security.

A copy of such order shall be served upon the person so prohibited as per Rule 8 of the FCR, Rule 2011, and thereupon the provisions of section 7 of the Unlawful Activities (Prevention) Act, 1967 shall, apply to, or in relation to, such article or currency or security and references in the said sub-sections to moneys, securities or credits shall be taken as references to such article or currency or security.

Action in respect of article, currency or security received in contravention of the Act.

- (1) The Central Government may issue a prohibitory order for contravention of the Act in respect of any article, currency or securities.
- (2) The prohibitory order issued shall be served on the person concerned in the following manner-
 - (a) by delivering or tendering it to that person or to his duly authorised agent; or
 - (b) by sending it to him by 'registered post with acknowledgement due' or 'speed post' to the address of his last known place of residence or the place where he carries on, or is known to have last carried on, business or the place where he personally works for gain or is known to have last worked for gain and, in case the person is an organisation or an association, to the last known address of the office of such organisation or association; or
 - (c) if it cannot be served in any of the manner aforesaid, by affixing it on the outer door or some other conspicuous part of the premises in which that person resides or carries on, or is known to have last carried on, business or personally works for gain, or is known to have last worked personally for gain and, in case the person is an organisation or an association, on the outer door or some other conspicuous part of the premises in which the office of that organisation or association is located, or is known to have been last located, and the written report whereof should be witnessed by at least two persons.



4. REGISTRATION

The provisions related to registration of persons for acceptance of foreign contribution, grant of certificate, its suspension, cancellation and renewal are dealt in chapter III of the FCRA. It covers sections 11 to 16 of the Act.

There are two modes of accepting the foreign contribution according to FCRA, 2010-

Mode I

- By **Registration** (Section 11(1)) - Registration is granted to only such persons which have been in existence for three years, have the audited financials of the past three years and spent at least INR 15 lacs, excluding administrative expenses.

Mode II

- Through **Prior Permission** (Section 11(2)) - Any organization which is in formative stage and is not eligible for certificate of registration may apply for prior permission, for receipt of a specific amount from specific donor/donors for carrying out specific activities/projects.

(I) Registration of certain persons with Central Government (Section 11)

(1) No person having a definite cultural, economic, educational, religious or social programme- shall accept foreign contribution unless such person obtains a certificate of registration from the Central Government.

[**Note:** However, any association registered with the Central Government under section 6, or granted prior permission under that section of the Foreign Contribution (Regulation) Act, 1976, as it stood immediately before the commencement of this Act, shall be deemed to have been registered or granted prior permission, as the case may be, under this Act and such registration shall be valid for a period of **five years** from the date on which this section comes into force – **this was a one time relief granted to such persons which were “registered” or granted “prior permission” under the erstwhile FCRA, 1976.**]

(2) Acceptance of foreign contribution after obtaining prior permission of the Central Government: Every person may, if it is not registered with the Central Government, accept any foreign contribution only after obtaining the prior permission of the Central Government and such prior permission shall be valid for the specific purpose for which it is obtained and from the specific source.

Forms for Application under Section 11⁴: An application for certificate of **registration** by a person under Section 11(1) for acceptance of foreign contribution shall be made in electronic form in Form FC-3A with an affidavit executed by each office bearer and key functionary and member in Proforma 'AA'.

An application for obtaining **prior permission** by a person under Section 11(2), for acceptance of foreign contribution, shall be made in electronic form in Form FC-3B with an affidavit executed by each office bearer and key functionary and member in Proforma 'AA' appended to these rules.

Any person making an application for registration shall have an FCRA Account.

⁴ Regulation - 9, Foreign Contribution (Regulation) Rules, 2011

If the Central Government, on the basis of any information or report, and after holding a summary inquiry, has reason to believe that a person who has been granted prior permission has contravened any of the provisions of this Act, it may, pending any further inquiry, direct that such person shall not utilise the unutilised foreign contribution or receive the remaining portion of foreign contribution which has not been received or, as the case may be, any additional foreign contribution, without prior approval of the Central Government.

Further, if the person has been found guilty of violation of any of the provisions of this Act or the Foreign Contribution (Regulation) Act, 1976, the unutilised or unreceived amount of foreign contribution shall not be utilised or received, as the case may be, without the prior approval of the Central Government.

(3) The Central Government may, by notification in the Official Gazette, specify—

- (i) the person or class of persons who shall obtain its prior permission before accepting the foreign contribution; or
- (ii) the area or areas in which the foreign contribution shall be accepted and utilised with the prior permission of the Central Government; or
- (iii) the purpose or purposes for which the foreign contribution shall be utilised with the prior permission of the Central Government; or
- (iv) the source or sources from which the foreign contribution shall be accepted with the prior permission of the Central Government.

The person may open one or more accounts in one or more banks for the purpose of utilising the foreign contribution after it has been received and, in all such cases, intimation in electronic form in Form FC-6D shall be furnished to the Secretary, Ministry of Home Affairs, New Delhi within fifteen days of the opening of any account.

Illustration: Can a private limited company or a partnership firm get registration or prior permission under FCRA, 2010?

Answer: Yes, a private limited company, provided the same is registered as a section 8 company under the Companies Act, 2013 may seek prior permission/registration for receiving foreign funds. Partnership Firm is not permitted to obtain registration or prior permission.

Illustration: Whether an individual or a Hindu Undivided Family (HUF) can be given registration or prior permission to accept foreign contribution in terms of section 11 of FCRA, 2010?

Answer: Yes. The definition of the 'person' in the Foreign Contribution (Regulation) Act, 2010 includes any individual and 'Hindu Undivided Family' among others. As such an Individual or an HUF is also eligible to apply for prior permission to accept foreign contribution.

Illustration: Whether organisations under Central/State Governments are required to obtain registration or prior permission under FCRA, 2010 for accepting foreign contribution?

Answer: Yes. However, all bodies constituted or established by or under a Central Act or a State Act requiring to have their accounts compulsorily audited by Comptroller & Auditor General of India are exempted from all the provisions of FCRA, 2010.

(II) Grant of certificate of registration (Section 12)

1. Conditions to be met for the grant of registration and prior permission

(1) An application by a person, referred to in section 11 for grant of certificate or giving prior permission, shall be made to the Central Government in such form and manner and along with such fee, as may be prescribed under Rule 9 of the Foreign Contribution (Regulation) Rules, 2011.

In terms of Section 12 (4) of FCRA, 2010, the following shall be the conditions for the grant of registration and prior permission:

- (a) The 'person' making an application for registration or grant of prior permission-
 - i. is not fictitious or benami;
 - ii. has not been prosecuted or convicted for indulging in activities aimed at conversion through inducement or force, either directly or indirectly, from one religious faith to another;
 - iii. has not been prosecuted or convicted for creating communal tension or disharmony in any specified district or any other part of the country;
 - iv. has not been found guilty of diversion or mis-utilisation of its funds;
 - v. is not engaged or likely to engage in propagation of sedition or advocate violent methods to achieve its ends;
 - vi. is not likely to use the foreign contribution for personal gains or divert it for undesirable purposes;
 - vii. has not contravened any of the provisions of this Act;
 - viii. has not been prohibited from accepting foreign contribution;
- (b) the person making an application for registration under sub-section (1) has undertaken reasonable activity in its chosen field for the benefit of the society for which the foreign contribution is proposed to be utilised;
- (c) the person making an application for giving prior permission under sub-section (1) has prepared a reasonable project for the benefit of the society for which the foreign contribution is proposed to be utilised;
- (d) the person being an individual, such individual has neither been convicted under any law for the time being in force nor any prosecution for any offence is pending against him.

- (e) the person being other than an individual, any of its directors or office bearers has neither been convicted under any law for the time being in force nor any prosecution for any offence is pending against him.
- (f) the acceptance of foreign contribution by the association/ person is not likely to affect prejudicially -
 - i. the sovereignty and integrity of India;
 - ii. the security, strategic, scientific or economic interest of the State;
 - iii. the public interest;
 - iv. freedom or fairness of election to any Legislature;
 - v. friendly relation with any foreign State;
 - vi. harmony between religious, racial, social, linguistic, regional groups, castes or communities.
- (g) the acceptance of foreign contribution-
 - i. shall not lead to incitement of an offence;
 - ii. shall not endanger the life or physical safety of any person.

2. Procedure for grant of certificate of Registration / Prior Permission

Application to be made to the Central Government (CG) in form FC-3A or FC-3B, as the case may be

CG on receipt of duly filled application, may register such person within 90 days and grant a certificate/give prior permission

In case of refusal, CG shall record the reasons and furnish the copy to the applicant

Certificate of Registration is valid for a period of 5 years and Prior Permission is valid upto the time the specific purpose/specific amount is fulfilled

- (1) **Application for Registration/ Prior Permission:** An application by a person, referred to in section 11 for grant of certificate or giving prior permission, shall be made to the Central Government in such form and manner and along with such fee, as may be prescribed.

Every person who makes an application under sub-section (1) shall be required to open "FCRA Account" in the manner specified in section 17 and mention details of such account in his application.

- (2) **Rejection of Application:** On receipt of an application the Central Government shall, by an order, if the application is not in the prescribed form or does not contain any of the particulars specified in that form, reject the application.
- (3) **Grant of Certificate of Registration /Prior Permission:** If on receipt of an application for grant of certificate of registration or giving prior permission and after making such inquiry as the Central Government deems fit, it is of the opinion that the conditions specified in sub-section (4) are satisfied, it may, ordinarily within ninety days from the date of receipt of application, register such person and grant him a certificate or give him prior permission, as the case may be, subject to such terms and conditions as may be prescribed.

If the Central Government does not grant, within the said period of ninety days, a certificate or gives prior permission, it shall communicate the reasons therefor to the applicant.

Note: A person shall not be eligible for grant of certificate or prior permission, if his certificate has been suspended and such suspension of certificate continues on the date of making application.

- (4) **Refusal to grant certificate of Registration /Prior Permission and furnishing of reasons therefor by Central Government:** Where the Central Government refuses the grant of certificate or does not give prior permission, it shall record in its order the reasons therefor and furnish a copy thereof to the applicant.

However, the Central Government may not communicate the reasons for refusal for grant of certificate of registration or for not giving prior permission to the applicant under this section, in cases where there is no obligation to give any information or documents or records or papers under the Right to Information Act, 2005.

- (5) **Validity of Certificate:** The certificate of Registration granted shall be valid for a period of five years from the date of its issue and the prior permission shall be valid for the specific purpose or specific amount of foreign contribution proposed to be received, as the case may be.

No person shall prefer a second application for registration or prior permission within a period of six months after submitting an application either for the grant of prior permission for the same project or for registration.

Permission for receipt of foreign contribution in application for obtaining prior permission.

As per Rule 9A of the Foreign Contribution (Regulation) Rules, 2011 If the value of foreign contribution on the date of final disposal of an application for obtaining prior permission is over rupees one crore, the Central Government may permit receipt of foreign contribution in such instalments, as it may deem fit.

Provided that the second and subsequent instalment shall be released after submission of proof of utilisation of seventy five per cent. of the foreign contribution received in the previous instalment and after field inquiry of the utilisation of foreign contribution.

Power of Central Government to require Aadhaar number, etc., as identification document: [Section 12A]

Notwithstanding anything contained in this Act, the Central Government may require that any person who seeks

- a. prior permission or prior approval under section 11, or
- b. makes an application for grant of certificate under section 12, or,
- c. as the case may be, for renewal of certificate under section 16,

shall provide an identification document.

For citizens of India, the Aadhaar number of all its office bearers or Directors or other key functionaries, by whatever name called, issued under the Aadhaar (Targeted Delivery of Financial and Other Subsidies, Benefits and Services) Act, 2016 shall be provided.

In case of a foreigner, a copy of the Passport or Overseas Citizen of India (OCI) Card shall be provided,

(III) Suspension of certificate (Section 13)

- (1) **Circumstances when certificate may be suspended:** The Central Government while considering the cancellation of a certificate on any of the grounds mentioned in Section 14(1) shall be satisfied that, it is necessary to suspend the certificate.

Period of suspension of certificate: Then, it may, by order in writing, suspend the certificate for a period of one hundred and eighty days, or such further period, not exceeding one hundred and eighty days, as may be specified.

- (2) **Effect of suspension:** Every person whose certificate has been suspended shall—

- (a) **not receive any foreign contribution** during the period of suspension of certificate.
However, the Central Government may, on an application made by such person, if it considers appropriate, allow receipt of any foreign contribution by such person on such terms and conditions as it may specify;
- (b) Not utilise, in the prescribed manner, the foreign contribution in his custody without the prior approval of the Central Government.

Rule 14 of FCR, Rules 2011 defines the extent of amount that can be utilised in case of suspension of the certificate of registration. The unspent amount that can be utilised in case of suspension of a certificate of registration may be as under:—

- (a) In case the certificate of registration is suspended under sub-section (1) of section 13 of the Act, up to twenty-five per cent of the unutilised amount may be spent, with the prior approval of the Central Government, for the declared aims and objects for which the foreign contribution was received.
- (b) The remaining seventy-five per cent of the unutilised foreign contribution shall be utilised only after revocation of suspension of the certificate of registration.

(IV) Cancellation of certificate (Section 14)

(1) Grounds for Cancellation of certificate

The Central Government may, by an order, cancel the certificate if the holder of the certificate has—

- (a) made an incorrect or false statement in, or in relation to, the application for the grant of registration or renewal thereof; or
 - (b) violated any of the terms and conditions of the certificate or renewal thereof; or
 - (c) violated any of the provisions of this Act or rules or order made thereunder; or
 - (d) if the holder of the certificate has not been engaged in any reasonable activity in its chosen field for the benefit of the society for two consecutive years or has become defunct.
 - (e) in the opinion of the Central Government, it is necessary in the public interest to cancel the certificate; or
- (2) No order of cancellation of certificate under this section shall be made unless the person concerned has been given a reasonable opportunity of being heard.
- (3) **Cooling period of three years:** Any person whose certificate has been cancelled under this section shall not be eligible for registration or grant of prior permission for a period of three years from the date of cancellation of such certificate.

GROUND'S FOR CANCELLATION OF CERTIFICATE BY CG -

Incorrect or false statement in application

Violation of any of the terms and conditions of the certificate

It is necessary in the public interest

Not engaged in any reasonable activity for two consecutive years

Violation of any of the provisions of this Act /rules / order

(V) Surrender of certificate (Section 14A)

- (1) A request may be made to the Central Government for surrender of certificate.
- (2) The Central Government shall make such inquiry as it deems fit and satisfy itself that such person has not contravened any of the provisions of this Act, and the management of foreign contribution and asset, if any, created out of such contribution has been vested in the authority as provided in sub-section (1) of section 15.
- (3) Thereafter the Central Government may permit any person to surrender the certificate granted under this Act.

⁵The validity of certificate surrendered under section 14A of the Act shall be deemed to have expired on the date of acceptance of the request by the Central Government.

⁶Voluntary surrender of certificate

Every person who has been granted certificate of registration under section 12 of the Act may make an application in electronic form in Form FC-7 for surrender of the certificate of registration in terms of section 14A of the Act.

(VI) Management of foreign contribution of person whose certificate has been cancelled or surrendered (Section 15)

- (1) **Vesting of custody:** The foreign contribution and assets created out of the foreign contribution in the custody of every person whose certificate has been cancelled or surrendered shall vest in banking authority concerned till the Central Government issues further directions in the matter as per Rule 15 of the FCR Rules, 2011.

Custody of foreign contribution in respect of a person whose certificate has been cancelled.

If the certificate of registration of a person who has opened an FCRA Account under section 17 is cancelled, the amount of foreign contribution lying unutilised in that Account shall vest with the prescribed authority under the Act.

- (2) **Role of Authority:** Such an authority may, if it considers necessary and in public interest manage the activities of the person, as the Central Government may direct and such authority may utilise the foreign contribution or dispose of the assets created out of it in case adequate funds are not available for running such activity.
- (3) **Return of vested Foreign Contribution & assets:** The concerned authority shall return the foreign contribution and the assets vested upon it to the person, if such person is subsequently registered under this Act.

⁵ Regulation - 10, Foreign Contribution (Regulation) Rules, 2011

⁶ Regulation - 15A, Foreign Contribution (Regulation) Rules, 2011.

(VII) Renewal of certificate (Section 16)

- (1) **Period for applying for renewal of certificate:** Every person who has been granted a certificate, shall have such certificate renewed within six months before the expiry of the period of the certificate.
- (2) ⁷Filing of an application to CG: An application for renewal of the certificate of registration shall be made to the Central Government in electronic form in Form FC-3C accompanied with an affidavit executed by each office bearer, key functionary and member in Proforma 'AA' appended to these rules within six months before the date of expiry of the certificate of registration.

Every person seeking renewal of the certificate of registration under section 16 of the Act shall open an FCRA Account and mention details of the account in his application for renewal of registration.

An application made for renewal of the certificate of registration shall be accompanied by a fee of rupees five thousand only, which shall be paid through payment gateway specified by the Central Government.

No person whose certificate of registration has ceased to exist shall either receive or utilise the foreign contribution until the certificate is renewed.

If no application for renewal of registration is received or the application is not accompanied by requisite fee before the expiry of the validity of the certificate of registration, the validity of the certificate of registration shall be deemed to have ceased from the date of completion of the period of five years from the date of the grant of certificate of registration.

Note 1: A certificate of registration granted on the 1st January, 2017 shall be valid till the 31st December, 2022 and a request for renewal of certificate of registration shall be submitted in electronic form accompanied by requisite fee after the 30th June, 2022 and within the 31st December, 2022.

Note 2: If no application is received or is not accompanied by renewal fee, the validity of the certificate of registration issued on the 1st January 2017 shall be deemed to have ceased after the 31st December, 2022 and the applicant shall neither receive nor utilise the foreign contribution until the certificate of registration is renewed, from 1st January 2023 onwards.

The amount of foreign contribution lying unutilised in the FCRA Account and utilisation account of a person whose certificate of registration is deemed to have ceased under sub-rule (6) and assets, if any, created out of the foreign contribution, shall vest with the prescribed authority under the Act until the certificate is renewed or fresh registration is granted by the Central Government.

⁷ Regulation - 12, Foreign Contribution (Regulation) Rules, 2011

If the validity of the certificate of registration of a person has ceased in accordance with the provisions of these rules, a fresh request for the grant of a certificate of registration may be made by the person to the Central Government as per the provisions of rule 9.

Illustration 12: A certificate of registration was granted to an NGO on the 1st January, 2014. A request for renewal of the certificate was received by the Central Government, by the 30th June, 2018. But the request was not accompanied by the renewal fee. Comment on the validity of the registration certificate issued on 1st January 2014.

Answer: A certificate of registration granted on the 1st January, 2014 shall be valid till the 31st December, 2018. A request for renewal of the registration certificate shall reach the Central Government, accompanied by the requisite fee, by the 30th June, 2018. In the instant case although an application has been made it was not accompanied by the renewal fee, the validity of the registration certificate issued on the 1st January 2014 shall be deemed to have lapsed with effect from the close of the day on 31st December, 2018.

- (3) **Period for renewal of certificate:** The Central Government shall renew the certificate, ordinarily within **ninety days** from the date of receipt of application for renewal of certificate subject to such terms and conditions as it may deem fit and grant a certificate of renewal for a period of five years.

The Central Government may, before renewing the certificate, make such inquiry, as it deems fit, to satisfy itself that such person has fulfilled all conditions specified in sub-section (4) of section 12. (Discussed earlier).

However, in case the Central Government does not renew the certificate within the said period of ninety days, it shall communicate the reasons therefor to the applicant.

The Central Government may refuse to renew the certificate in case where a person has violated any of the provisions of this Act or rules made thereunder.

- (4) **Procedure where certificate has lapsed or ceased to be valid:**⁸ If the validity of the certificate of registration of a person has ceased in accordance with the provisions of Rule 12 a fresh request for the grant of a certificate of registration may be made by the person to the Central Government as per the provisions of rule 9 (Discussed earlier).

In case a person provides sufficient grounds, in writing, explaining the reasons for not submitting the certificate of registration for renewal within the stipulated time, his application may be accepted for consideration along with the requisite fee and with late fee of 5,000/-, but not later than one year after the expiry of the original certificate of registration.

⁸ Sub Rules (7) and (8) of Rule 12 of the Foreign Contribution (Regulation) Rules, 2011.



5. ACCOUNTS, INTIMATION, AUDIT AND DISPOSAL OF ASSETS, ETC.

Chapter IV of the Act deals with incidental and consequential matters such as opening of a designated "FCRA Account, maintenance of accounts, provision of information and disposal of assets. It covers sections 17 to 22 of the Act.

(I) Foreign contribution through scheduled bank (Section 17)

Every person who has been granted certificate or prior permission under section 12 shall receive foreign contribution only in an account designated as "FCRA Account" by the bank,

Such "FCRA Account" shall be opened by him for the purpose of remittances of foreign contribution in such branch of the State Bank of India at New Delhi, as the Central Government may, by notification, specify in this behalf:

Provided that such person may also open another "FCRA Account" in a scheduled bank of his choice for the purpose of keeping or utilising the foreign contribution which has been received from his "FCRA Account" in the specified branch of State Bank of India at New Delhi:

Provided further that such person may also open one or more accounts in one or more scheduled banks of his choice to which he may transfer for utilising any foreign contribution received by him in his "FCRA Account" in the specified branch of the State Bank of India at New Delhi or kept by him in another "FCRA Account" in a scheduled bank of his choice:

No funds other than foreign contribution shall be received or deposited in any such account.

The specified branch of the State Bank of India at New Delhi or the branch of the scheduled bank where the person referred to in sub-section (1) has opened his foreign contribution account or the authorised person in foreign exchange, shall report to such authority as may be specified, -

- (a) the prescribed amount of foreign remittance;
- (b) the source and manner in which the foreign remittance was received; and
- (c) other particulars,

in such form and manner as may be prescribed.

Reporting by banks of receipt of foreign contribution. ⁹The bank shall report to the Central Government within forty-eight hours any transaction in respect of receipt or utilisation of any foreign contribution by any person whether or not such person is registered or granted prior permission under the Act.

⁹ Rule 16 of the Foreign Contribution (Regulation) Rules, 2011.

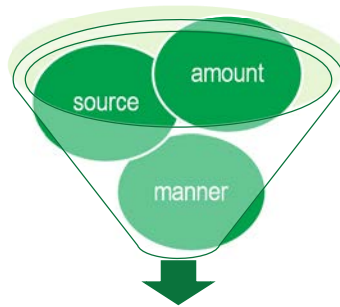
The aim of the new Section 17, substituted by the FCR Amendment Act, 2020, appears to be to ensure that all foreign contribution received into the country is routed through the State Bank of India at New Delhi. The recipient may also open other accounts with scheduled banks of his choice for operational convenience. Initial receipt shall be into the FCRA Account with designated branch of State Bank of India, New Delhi. Later the amount may be transferred to another account with scheduled bank of choice. Further transfers to "other" accounts with Scheduled banks of choice for utilisation is also permitted. This somewhat cumbersome procedure would, apparently, ensure tighter monitoring both at source as well as destination of the Foreign Contribution.

Illustration: Can foreign contribution be mixed with local receipts?

Answer: No. Foreign contribution cannot be deposited or utilised from the bank account being used for domestic funds.

(II) Intimation (Section 18)

Every person who has been granted a certificate or given prior approval shall give an intimation to the Central Government, and such other authority as may be specified by the Central Government.



CG shall be intimated by every person of the AMOUNT such foreign contribution received, the SOURCE from which and the MANNER in which such foreign contribution was received and the PURPOSES for which, and the MANNER in which such foreign contribution was utilised by him.

Every person receiving foreign contribution shall submit a copy of a statement with the particulars of foreign contribution received duly certified by officer of the bank or authorised person in foreign exchange and furnish the same to the Central Government along with the intimation.

Intimation of foreign contribution by the recipient.

- (1) Every person who receives foreign contribution under the Act, shall submit a signed or digitally signed report in electronic form in Form FC-4 with scanned copies of income and expenditure statement, receipt and payment account and balance sheet for every financial year beginning on the 1st day of April within nine months of the closure of the financial year.
- (2) The annual return in Form FC-4 shall reflect the foreign contribution received in the exclusive bank account and include the details in respect of the funds transferred to other bank accounts for utilisation.

- (3) If the foreign contribution relates only to articles, the intimation shall be submitted in Form FC-1.
- (4) If the foreign contribution relates to foreign securities, the intimation shall be submitted in Form FC-1.
- (5) Every report submitted under sub-rules (2) to (4) shall be duly certified by a chartered accountant.
- (6) Every such return in Form FC-4 shall also be accompanied by a copy of a statement of account from the bank where the exclusive foreign contribution account is maintained by the person, duly certified by an officer of such bank.
- (7) The accounting statements referred to above in the preceding sub-rule shall be preserved by the person for a period of six years.
- (8) A 'NIL' report shall be furnished even if no foreign contribution is received during a financial year:

Provided that where foreign contribution has not been received or utilised during a financial year, it shall not be required to enclose certificate from Chartered Accountant or income and expenditure statement or receipt and payment account or balance sheet with Form FC-4.

(III) Maintenance of accounts (Section 19)

Every person who has been granted a certificate or given prior approval under this Act shall maintain, in such form and manner as may be prescribed,—

- (a) an account of any foreign contribution received by him; and
- (b) a record as to the manner in which such contribution has been utilised by him.

Rule 11 of FCR, Rule 2011 states that every person who has been granted registration or prior permission under section 12 shall maintain a separate set of accounts and records, exclusively, for the foreign contribution received and utilised.

(IV) Audit of accounts (Section 20)

- (1) Where any person who has been granted a certificate or given prior permission,
 - a. fails to furnish any intimation under this Act, or
 - b. the intimation so furnished is not in accordance with law or
 - c. if, after inspection of such intimation, the Central Government has any reasonable cause to believe that any provision of this Act has been, or is being, contravened,

the Central Government may-

- by general or special order, authorise such Gazetted Officer, holding a Group A post under the Central Government or any other officer or authority or organisation, as it may think fit.
 - to audit any books of account kept or maintained by such person.
- (2) Every such officer shall have the right to enter in or upon any premises at any reasonable hour, before sunset and after sunrise, for the purpose of auditing the said books of account.
 - (3) Any information obtained from such audit shall be kept confidential and shall not be disclosed except for the purposes of this Act.

(V) Intimation by candidate for election (Section 21)

Every candidate for election, who had received any foreign contribution, at any time within **one hundred and eighty days** immediately preceding the date on which he is duly nominated as such candidate, shall give, within such time and in such manner as may be prescribed, an intimation to the Central Government or prescribed authority or both as to the amount of foreign contribution received by him, the source from which, and the manner in which, such foreign contribution was received and the purposes for which and the manner in which such foreign contribution was utilised by him.

Foreign contribution received by a candidate for election

As per Regulation 18 of FCR, Rule 2011, foreign contribution received by a candidate for election, shall be furnished in Form FC-1 in electronic form within forty-five days from the date on which he is duly nominated as a candidate for election.

(VI) Disposal of assets created out of foreign contribution (Section 22)

Where any person who was permitted to accept foreign contribution under this Act-

- (a) **ceases to exist or has become defunct** – in this case all the assets of such person shall be disposed of in accordance with the provisions contained in any law for the time being in force under which the person was registered or incorporated, and
- (b) **in the absence of any such law**- the Central Government may, having regard to the nature of assets created out of foreign contribution received under this Act, by notification, specify that all such assets shall be disposed of by such authority, in such manner and procedure as may be prescribed.



6. ADJUDICATION

Chapter VI of the Act deals with Adjudication. It covers sections 28 to 30 of the Act.

Confiscation of article or currency or security obtained in contravention of the Act (Section 28)

Any article or currency or security which is seized under the Act shall be liable to confiscation if such article or currency or security has been adjudged under section 29 to have been received or obtained in contravention of this Act.

Adjudication of confiscation (Section 29)

- (1) Any confiscation referred to in section 28 may be adjudged—
- without limit, by the Court of Session** within the local limits of whose jurisdiction the seizure was made; and
 - subject to such limits as may be prescribed**, by such officer, not below the rank of an Assistant Sessions Judge, as the Central Government may, by notification in the Official Gazette, specify in this behalf.

As per Rule 19 of FCR, Rule 2011 an officer referred to above in clause 29(1)(b), may adjudge confiscation in relation to any article or currency seized under the Act, if the value of such article or the amount of such currency seized does not exceed Rs. 10,00,000 (Rupees Ten lakh only).

- (2) When an adjudication is concluded by the Court of Session/Assistant Sessions Judge, as the case may be, he/she may make such order as he/she thinks fit for disposal of seized article or currency or security (i.e.) either
- confiscation of seized article or currency or security which has been used for the commission of any offence under this Act, or
 - delivery to any person claiming to be entitled to possession thereof or otherwise.

Procedure for confiscation (Section 30)

Reasonable opportunity of making a representation has to been given to the person from whom any article or currency or security has been seized prior to passing the order of adjudication of confiscation.

**7. APPEAL & REVISION**

Chapter VIII of the Act deals with Appeal & Revision. It covers sections 31 and 32 of the Act.

Appeal (Section 31)

- (1) Any person aggrieved by any order made under Section 29 may prefer an appeal as follows:

Where an order is passed by-	Appellate Authority
the Court of Session	The High Court to which such Court is subordinate

any officer specified section 29(1)(b)	The Court of Session within the local limits of whose jurisdiction such order of adjudication of confiscation was made
Appeal is to be preferred within one month from the date of communication of the order to such person.	
The appellate court may allow such appeal to be preferred for a further period of one month.	

- (2) Any organisation referred to in section 3(1)(f), or any person or association referred to in section 6 or section 9, aggrieved by an order made in pursuance of section 5 or by an order of the Central Government refusing to give permission under this Act, or by any order made by the Central Government under section 12(2) or 12(4), or section 14(1), as the case may be, may,
- prefer an appeal against such order to the High Court within the local limits of whose jurisdiction the appellant ordinarily resides or carries on business or personally works for gain, or, where the appellant is an organisation or association, the principal office of such organisation or association is located-
 - within sixty days from the date of such order.

The above appellate remedy is available to organisations

- that have been adjudged to be Political in nature under Section 5;
 - that have been refused grant of registration; or
 - whose registration has been cancelled
- by Central government.

Revision of orders by Central Government (Section 32)

- (1) The Central Government may either-
- of its own motion or
 - on an application for revision by the person registered under this Act,
- call for and examine the record of any proceeding under this Act in which any such order has been passed by it and may make such inquiry or cause such inquiry to be made and, subject to the provisions of this Act, may pass such order thereon as it thinks fit.
- (2) **Time limit for power of revision:** The Central Government shall not of its own motion revise any order under this section if the order has been made **more than one year previously**.
- (3) **Time limit for making application for revision:** In the case of an application for revision by a person registered under the act, the application must be made **within one year** from the

date on which the order in question was communicated to him or the date on which he otherwise came to know of it, whichever is earlier.

If the Central Government is satisfied that such person was prevented by sufficient cause from making the application within that period it may admit an application made after the expiry of that period.

- (4) The Central Government shall revise any order where an appeal against the order lies but has not been made until the time within which such appeal may be made has expired or such person has waived his right of appeal or an appeal has been filed under this Act.
- (5) Every application by such person for revision under this section shall be accompanied by such fee, as may be prescribed.

An order by the Central Government declining to interfere shall, for the purposes of this section, be deemed not to be an order prejudicial to such person. This means that the applicant has no right of appeal against the declining to interfere.

As per Regulation 20 of the FCR Rule 2011, an application for revision of an order passed by the competent authority under section 32 of the Act shall be made to the Secretary, Ministry of Home Affairs, Government of India, New Delhi in such form and manner, including in electronic form as may be specified by the Central Government and it shall be accompanied by a fee of rupees three thousand only, which shall be paid through the payment gateway specified by the Central Government.

In exercise of the powers under rule 20 of the Foreign Contribution (Regulation) Rules, 2011 as amended vide gazette notification No. 506(E), dated 1-7-2022, it is hereby ordered that w.e.f. 1st September 2022 an application under section 32 of the Act for revision of an order passed by the competent authority shall be made in electronic form only through the website <https://fcraonline.nic.in>.



8. OFFENCES AND PENALTIES

Chapter VII of the Act deals with Offences & Penalties. It covers sections 33 to 41 of the Act. This chapter lists out various types of offences committed and prescribes the penalties levied for the same.

Types of offences (Sections 33-38)

Section	Type of offence	Penalty
	Any person who knowingly— (a) gives false intimation under section 9(c) or section 18; or (b) seeks prior permission or	shall, on conviction by a court, be liable to imprisonment for a term which may extend to six months or with fine or with both.

33	registration by means of fraud, false representation or concealment of material fact,	
34	Any person, on whom any prohibitory order has been served under section 10, pays, delivers, transfers or otherwise deals with, any article or currency or security, whether Indian or foreign, in contravention of such prohibitory order.	• shall be punished with imprisonment for a term which may extend to three years, or with fine, or with both. • the court trying such contravention may also impose on the person convicted an additional fine equivalent to the market value of the article or the amount of the currency or security in respect of which the prohibitory order has been contravened by him or such part thereof as the court may deem fit.
35	Whoever accepts, or assists any person, political party or organisation in accepting, any foreign contribution or any currency or security from a foreign source, in contravention of any provision of this Act or any rule or order made thereunder	shall be punished with imprisonment for a term which may extend to five years, or with fine, or with both.
36	The court trying a person, who, in relation to any article or currency or security, whether Indian or foreign, does or omits to do any act which act or omission would render such article or currency or security liable to confiscation under this Act, may, in the event of the conviction of such person for the act or omission aforesaid	impose on such person a fine not exceeding five times the value of the article or currency or security or one thousand rupees, whichever is more, if such article or currency or security is not available for confiscation, and the fine so imposed shall be in addition to any other fine which may be imposed on such person under this Act.
37	Whoever fails to comply with any provision of this Act for which no separate penalty has been provided in this Act	shall be punished with imprisonment for a term which may extend to one year, or with fine or with both.
	Second Conviction or Repeat	shall not accept any foreign

38	Offender: Any person having been convicted of any offence under section 35 or section 37, insofar as such offence relates to the acceptance or utilisation of foreign contribution, is again convicted of such offence	contribution for a period of five years from the date of the subsequent conviction.

Offences by companies (Section 39)

Where an offence under this Act or any rule or order made thereunder has been committed by a company-

- every person who, at the time the offence was committed, was in charge of, and
- was responsible to, the company for the conduct of the business of the company,
- as well as the company,

shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly.

Exemption: However, such person shall not be liable to any punishment if he proves that the offence was committed –

- without his knowledge, or
- he had exercised all due diligence to prevent the commission of such offence.

Where an offence under this Act or any rule or order made thereunder has been committed by a company and it is proved that the offence has been committed with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of that offence and shall be liable to be proceeded against and punished accordingly.

Explanation.—For the purposes of this section,—

- “company”** means any body corporate and includes a firm, society, trade union or other association of individuals; and
- “director”**, in relation to a firm, society, trade union or other association of individuals, means a partner in the firm or a member of the governing body of such society, trade union or other association of individuals.

Bar on prosecution of offences under the Act (Section 40)

No court shall take cognizance of any offence under this Act, except with the previous sanction of the Central Government or any officer authorised by that Government in this behalf.

Compounding of certain offences (Section 41)

- any offence punishable under this Act (whether committed by an individual or association or any officer or employee thereof), not being an offence punishable with imprisonment only,

may, before the institution of any prosecution, be compounded by such officers or authorities and for such sums as the Central Government may, by notification in the Official Gazette, specify.

- Compounding of offences as stated above, shall not apply to an offence committed by an individual or association or its officer or other employee within a period of three years from the date on which a similar offence committed by it or him was compounded under this section.

For the purposes of this section, any second or subsequent offence committed after the expiry of a period of three years from the date on which the offence was previously compounded, shall be deemed to be a first offence.

- Every officer or authority shall exercise the powers to compound an offence, subject to the direction, control and supervision of the Central Government.
- Where any offence is compounded before the institution of any prosecution, no prosecution shall be instituted in relation to such offence, against the offender in relation to whom the offence is so compounded.
- Every officer or authority while dealing with a proposal for the compounding of an offence for a default in compliance with any provision of this Act which requires by an individual or association or its officer or other employee to obtain permission or file or register with, or deliver or send to, the Central Government or any prescribed authority any return, account or other document, may-

direct, by order, any individual or association or its officer or other employee to file or register with, such return, account or other document within such time as may be specified in the order.



9. MISCELLANEOUS

(I) Power to call of information or document and Investigation into cases under the Act (Sections 42 & 43)

- Any inspecting officer, authorised by the Central Government may, during the course of any inspection of any account or record maintained by any political party, person, organisation or association in connection with the contravention of any provision of this Act,—
 - (a) call for information from any person for the purpose of satisfying himself whether there has been any contravention of the provisions of this Act or rule or order made thereunder;
 - (b) require any person to produce or deliver any document or thing useful or relevant to such inspection;

(c) examine any person acquainted with the facts and circumstances of the case related to the inspection.

- **Investigation into cases under the Act:** Any offence punishable under this Act may also be investigated into by such authority as the Central Government may specify in this behalf and the authority so specified shall have all the powers which an officer-in-charge of a police station has while making an investigation into a cognizable offence.

(II) Power of Central Government to give directions and delegation of powers (Sections 46 & 47)

- The Central Government may give such directions as it may deem necessary to any other authority or any person or class of persons regarding the carrying into execution of the provisions of this Act, except power to make rule under section 48.

(III) Power to make rules (Section 48)

The Central Government may, by notification, make rules for carrying out the provisions of this Act.

(IV) Power to exempt in certain cases (Section 50)

If the Central Government is of opinion that it is necessary or expedient in the interests of the general public so to do, it may-

- by order and subject to such conditions as may be specified in the order, exempt-
 - any person or
 - association or
 - organisation (not being a political party), or
 - any individual (not being a candidate for election)
- from the operation of all or any of the provisions of this Act and may, revoke or modify such order.

(V) Act not to apply to certain Government transactions (Section 51)

Nothing contained in this Act shall apply to any transaction between-

- the Government of India, and
- the Government of any foreign country or territory.

(VI) Application of other laws not barred (Section 52)

The provisions of this Act shall be in addition to, and not in derogation of, the provisions of any other law for the time being in force.

TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. *Alexander Philip, a foreign citizen, has made donations in kind to his known resident Indians for their personal use. When shall such donation in kind be excluded from the definition of 'foreign contribution' considering the relevant provisions of Foreign Contribution (Regulation) Act, 2010?*
 - (a) *A donation in kind by a foreign citizen to a resident Indian shall be excluded from the definition of 'foreign contribution', if the market value, in India, of such article, on the date of such gift, is more than ₹ 1,00,000 but less than ₹ 5,00,000.*
 - (b) *A donation in kind by a foreign citizen to a resident Indian shall be excluded from the definition of 'foreign contribution', if the market value, in India, of such article, on the date of such gift, is more than ₹ 5,00,000 but less than ₹ 10,00,000.*
 - (c) *Any donation in kind given by a foreign citizen to a resident Indian for personal use is always excluded.*
 - (d) *A donation in kind by a foreign citizen to a resident Indian shall be excluded from the definition of 'foreign contribution', if the market value, in India, of such article, on the date of such gift, is not more than ₹ 1,00,000.*

2. *Mr. Vijay, Sanjay and Ajay are brothers. Mr. Sanjay who is professor reside in India, rest both the brothers settled in abroad. Mr. Sanjay on his 25th wedding anniversary received a gift from his elder brother who is American national currently. Gift includes i-phone and an old chain of their father, with attached emotional memories. I-phone in Indian rupee worth INRs 1 lac 10 thousands, while chain worth INRs 80 thousand.*
While younger brother of Mr. Sanjay who is British national and investment banker by profession, present him securities worth INRs 2 lacs.
Regarding the intimation of foreign contribution received by Mr. Sanjay, state the correct legal requirement in the light of the FCRA :
 - (a) *Intimation is required to be given to Central Government regarding any of the foreign contribution received by him within three months from the date of receipt of such contribution.*
 - (b) *Intimation is required to be given to Central Government regarding the foreign contribution received by him with his brothers being more than limit of 1 Lakh within 30 days from the date of receipt of such contribution.*

- (c) *Intimation is not required to be given to Central Government regarding the foreign contribution received by him with his brothers being less than the threshold limit of 10 Lakh whereas w.r.t. to chain of worth INR 80,000.*
 - (d) *No Intimation is required to be given to Central Government regarding the foreign contribution received him as it was for personal use.*
3. *The Certificate of registration for receiving foreign contribution was issued on 1st April, 2023 to Mr. X . What shall be the validity period for said registration:*
- (a) *31st March 2025*
 - (b) *1st April 2026*
 - (c) *1st April, 2027*
 - (d) *31st March 2028*
4. *Mr Raja, an office-bearer of a political party, receives foreign contribution of Rs. 9 lakh during the financial year 2022-2023 from his sister residing abroad. Mr. Raja is required to inform of such foreign contribution received to the Central Government within how many time period:*
- (a) *With in 30 days from the date of receipt of such foreign contribution*
 - (b) *With in 3 months from the date of receipt of such foreign contribution*
 - (c) *With in 6 months from the date of receipt of such foreign contribution*
 - (d) *No intimation is required for such foreign contribution*
5. *Mr. X has been found guilty of violation of the provisions of FCRA, 2010. What shall be the consequences w.r.t. the unutilised amount of foreign contribution?*
- (a) *Such unutilised amount of foreign contribution shall be forfeited.*
 - (b) *Such unutilised amount of foreign contribution shall not be utilized, without the prior approval of the C.G*
 - (c) *Such unutilised amount of foreign contribution shall not be utilized without the prior approval of the RBI.*
 - (d) *Such unutilised amount of foreign contribution shall not be utilized till the settlement of penalty imposed*

Descriptive Questions

1. State under what circumstances Government can cancel the certificate of registration granted to a person under FCRA?
2. X, an association having registration wishes to transfer the Foreign Contribution received by it to another organization? Can it do so? Is there any restriction on transfer of funds to other organisations?
3. Can foreign contribution be received in and utilised from multiple Bank Accounts?
4. Can capital assets purchased with the help of foreign contributions be acquired in the name of the Mr Ram, an office bearer of the association?
5. Mr. X, an individual of Indian origin but currently a citizen of a foreign country gives a donation. State whether the donation given by Mr. X will be treated as 'foreign contribution'?
6. Mr. Rohit, a relative of Ms. Suman, who is residing in France remitted foreign contribution of Rs. 2 lakhs to her for arrangement of religious programme for the believers of Gurudev. Whether foreign remittances received from a relative are to be treated as foreign contribution as per FCRA, 2010?
7. After giving a reasonable opportunity of being heard, Central Government cancelled the certification of registration of Toastea Ltd, a company registered under FCRA on the ground that such cancellation was in public interest. Two and a half years have passed since such cancellation. Company has submitted its written declaration not to involve in such activities again and requests restoration of the registration. Advise Toastea Ltd. on its eligibility for re-registration or grant of prior permission.
8. In the light of the provisions of the Foreign Contribution (Regulation) Act, 2010 examine and decide whether the following persons in India are permitted to receive the amount/articles in the following situations:
 - (i) M/s KG & Co.; a partnership firm obtained loan from a club registered in London for its business purpose.
 - (ii) Hello FM, a registered association, received funds from a foreign company for establishing Frequency Model Radio Station to broadcast audio news.
 - (iii) Mr. Happy received a wrist watch as marriage anniversary gift from his uncle, a citizen of USA. The market value of the wrist watch is Rs. 25,000.
9. Mr. Ramakant Hathi, an Indian Administrative Service (IAS) officer has received an invitation to visit Germany for representing India in an Annual Summit programme. Mr. Ramakant Hathi, on his visit has met with a sudden illness and received foreign hospitality of amount equivalent to INR 65,000 in the form of emergent medical treatment. Under the given scenario, you are required to advise Mr. Ramakant Hathi regarding his responsibility to intimate the receipt of

Foreign Hospitality as per the provisions of the Foreign Contribution (Regulation) Act, 2010 and rules made thereunder.

10. *XYZ Foundation, a society registered under the Societies Registration Act, 1860, has received foreign contribution from a Mala Company LLC, a company incorporated in Singapore. XYZ Foundation deposited the amount of foreign contribution in a bank and earned interest on it. XYZ Foundation desires to invest maturity proceeds from deposits in mutual funds. You are required to advise whether XYZ Foundation is allowed to make such investment considering the provisions of the Foreign Contribution (Regulation) Act, 2010 (the Act) (Note: XYZ Foundation has obtained certificate of registration under section 11 of the Act).*

ANSWERS

Answer to Multiple Choice Questions

1.	d	2.	c	3.	d	4.	d	5.	b

Answer to Descriptive Answers

1. As per section 14 of the FCRA, Central Government may cancel the certificate, after carrying out an inquiry, on the following grounds –
 - (a) the holder of the certificate has made an incorrect/false statement in the application for the grant of registration or renewal
 - (b) the holder of the certificate has violated any of the terms and conditions of the certificate or renewal thereof
 - (c) in the opinion of the Central Government, it is necessary in the public interest to cancel the certificate
 - (d) the holder of the certificate has violated any of the provisions of this Act or rules or order made thereunder.
 - (e) if the holder of the certificate has not been engaged in any reasonable activity in its chosen field for the benefit of the society for two consecutive years or has become defunct.

Any person whose certificate has been cancelled under this section shall not be eligible for registration or grant of prior permission for a period of three years from the date of cancellation of such certificate.

2. As per amendment to Section 7 of FCRA, 2010, vide The Foreign Contribution (Amendment) Act, 2020;

No person who -

- (a) is registered and granted a certificate or has obtained prior permission under this Act; and
- (b) receives any foreign contribution,

shall transfer such foreign contribution to any other person.

Prior to amendment, foreign contribution could be transferred with the prior approval of the Central Government to such persons which did not possess the certificate of registration or prior permission. Further foreign contribution was also permitted to be transferred to any other person who was registered under FCRA, 2010 or had obtained prior permission. It can be seen that the legislature has placed a blanket prohibition on transfer of foreign contribution received by any person to any other person. The intention is to prevent recipients of foreign contribution acting as mere conduits or facilitating agents for obtaining foreign contributions.

3. Yes. The foreign contribution should be received only in the exclusive single "FCRA account" of New Delhi Main Branch of SBI (also called designated FC account), as mentioned in the order for registration or prior permission granted and shall be independently maintained by the associations. Besides, this "FCRA Account", the association may also open "another FCRA Account" in any scheduled bank of its choice & link these accounts for transfer of foreign contribution. Also, one or more accounts (called Utilization Account) in one or more scheduled banks may be opened by the association for 'utilising' the foreign contribution after it has been received in the designated FCRA bank account, provided that no fund other than foreign contribution shall be received or deposited in such account or accounts and in all cases of any change, intimation in FC-6D is to be given online within 45 days of opening of such account. .
4. No. Every asset purchased with foreign contribution should be acquired and possessed in the name of the association since an association has a separate legal entity distinct from its members.
5. Yes. Donation from a Person of Indian origin who has acquired foreign citizenship is treated as foreign contribution. This will also apply to Person of Indian Origin / Overseas Citizen of India cardholders. However, this will not apply to 'Non-resident Indians', who still hold Indian citizenship and they are not foreigners. Therefore, donation given by Mr. X, an individual of Indian origin with foreign nationality will be treated as foreign contribution.
6. No. As per Section 4(e) of FCRA, 2010 and Rule 6 of FCRR, 2011, even the persons prohibited under section 3, i.e., persons not permitted to accept foreign contribution, are allowed to accept foreign contribution from their relatives. However, in terms of Rule 6 of FCRR, 2011, any person receiving foreign contribution in excess of ten lakh rupees or equivalent thereto in a financial year from any of his relatives shall inform the Central

Government regarding the details of the foreign contribution received by him in electronic form in Form FC-1 within three months from the date of receipt of such contribution.

Here in the given situation, since the amount remitted by Mr. Rohit is less than Rs. ten lakh, so Ms. Suman is not required to inform the Central Government.

7. **Restoration of Registration:** As per section 14(3) of the Foreign Contribution (Regulation) Act, 2010, any person whose certificate has been cancelled under this section shall not be eligible for registration or grant of prior permission for a period of three years from the date of cancellation of such certificate.

In the instant case, Toastea Ltd. is not eligible for re-registration or grant of prior permission as only two and a half years have passed since such cancellation. So, restoration is not permissible as the requirement of three years cooling period from the date of cancellation of such certificate for re-registration is not complied with. Therefore Toastea Ltd. is advised to seek for fresh registration or grant of prior permission on the completion of three years from the date of cancellation.

8. (i) As per Explanation 3 to section 2(1)(h)—Any amount received, by any person from any foreign source in India, by way of fee (including fees charged by an educational institution in India from foreign student) or towards cost in lieu of goods or services rendered by such person in the ordinary course of his business, trade or commerce whether within India or outside India or any contribution received from an agent or a foreign source towards such fee or cost shall be excluded from the definition of foreign contribution within the meaning of this. Thus the loan availed from a club registered in London will be covered under business hence excluded from definition of foreign contribution. However, the provisions of FEMA, 1999 shall apply and permissibility of availing foreign currency loan by a partnership firm needs to be evaluated.
- (ii) As per section 3 of the FCRA, 2010, no foreign contribution shall be accepted by any association or company engaged in the production or broadcast of audio news or audio visual news or current affairs programs through any electronic mode, or any other electronic form as defined in the Information Technology Act, 2000 or any other mode of mass communication; Accordingly, Hello FM is not permitted to receive any funds from a foreign company.
- (iii) As per the provisions of the Foreign Contribution (Regulation) Act, 2010, “foreign contribution” means the donation, delivery or transfer made by any foreign source, of any article, not being an article given to a person as a gift for his personal use, if the market value, in India, of such article, on the date of such gift, is not more than such sum as may be specified from time to time, by the Central Government by the rules made by it in this behalf; (This sum has been specified as Rupees One lakh/-currently).

In the given situation, Mr. Happy received the wrist watch (market value Rs.25,000) as marriage anniversary gift from his uncle, a citizen of USA. Since, the value of the

wrist watch is within the prescribed limit, hence, Mr. Happy is permitted to receive the article.

9. As per section 6 of the Foreign Contribution (Regulation) Act, 2010, various categories of persons are required to take prior permission of the Central Government before accepting Foreign Hospitality, while visiting any country or territory outside India. Government servants are one of such persons who are required to take prior permission. Provided it shall not be necessary to obtain any such permission for an emergent medical aid needed on account of sudden illness contracted during a visit outside India.

Section 6 read along with Rule 7 of Foreign Contribution Rules 2011 and amendments thereto states that in case of emergent medical treatment aid needed on account of sudden illness during a visit abroad, the acceptance of foreign hospitality shall be required to be intimated to the Central Government within one month of such receipt in electronic form FC-2 giving full details including the source, approximate value in Indian rupees, and the purpose for which and the manner in which it was utilised. No such intimation is required if the value of such hospitality in emergent medical aid is upto one lakh rupees or equivalent.

Accordingly, Mr. Ramakant Hathi is not required to intimate such details of acceptance of foreign hospitality as the value of such hospitality in emergent medical treatment of foreign currency equivalent to INR 65,000 is within the limits specified in Rule 7 of Foreign Contribution (Regulation) Rules, 2011 of up to Rupees one lakh or equivalent.

10. As per section 8 of the Act, every person, who is registered and granted a certificate or given prior permission under this Act and receives any foreign contribution, shall utilise such contribution for the purpose for which the contribution has been received.

Further Rule 4 (1) of FCRR, 2011 defines speculative activities and includes instruments where there is an element of risk of appreciation or depreciation of the original investment.

Further as per the explanation 2 to the definition of foreign contribution under the Act, the interest accrued on the foreign contribution deposited in any bank referred to in section 17(1) or any other income derived from the foreign contribution or interest thereon shall also be deemed to be foreign contribution within the meaning of this clause.

Foreign contribution or any income arising out of it shall not be used for speculative business, where speculative business which includes investment in mutual fund.

Therefore, XYZ Foundation cannot use the foreign contribution or the interest earner on the foreign contribution for the Investment in Mutual Funds or for any speculative activities.

[illegible]

CHAPTER

3

THE INSOLVENCY AND BANKRUPTCY CODE, 2016



LEARNING OUTCOMES

At the end of this Chapter, you will be able to:

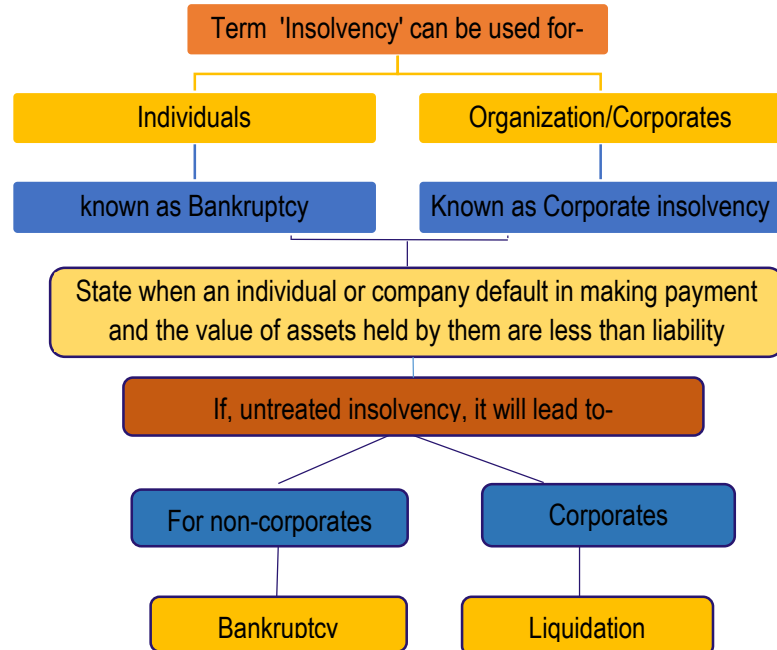
- ☐ Explain the concepts of Insolvency and Bankruptcy Code, 2016 (Code)
- ☐ Explain the relationship between Bankruptcy, Insolvency and Liquidation
- ☐ Explain the important terminologies used in the Code.
- ☐ Identify the structure and applicability of the Code.
- ☐ Elaborate the manner and process of Insolvency Resolution Process for Corporate Persons



1. INTRODUCTION

Concept of Insolvency and Bankruptcy

- The term insolvency is used for both individuals and organizations. Insolvency is when there is a default in payment and it's not paid. Default is defined under section 3(12) of the Insolvency and Bankruptcy Code, 2016. Untreated insolvency will lead to bankruptcy for non-corporates and liquidation of corporates. Creditors put money into debt investments today in return for the promise of fixed future cash flows. But the returns expected on these investments are still uncertain because at the time of repayment, the corporate or individual (debtor) may make repayments as promised, or he may default and does not make the payment. When default happens in payment, the debtor is considered insolvent. The debtor may be insolvent because of:
 - Financial Failure:** a persistent mismatch between payments by the enterprise and receivables into the enterprise, even though the business model is generating revenues, or
 - Business Failure:** which is a breakdown in the business model of the enterprise, and it is unable to generate sufficient revenues to meet payments¹ or there may be avoidance of transaction because of which also insolvency may have happened.



¹ The Report of the Bankruptcy Law Reforms Committee Volume I: Rationale and Design, November 2015

- From the above it is evident that insolvency is a state and bankruptcy is a conclusion. A bankrupt would be a conclusive insolvent whereas all insolvencies will not lead to bankruptcies. Insolvency situation can be resolved through resolution mechanism under the Code and a failed resolution mechanism would lead to liquidation process in relation to corporates and bankruptcy process in relation to individuals under the Code.
- **Avoidance Transactions:** It is covered in Chapter III of IBC, 2016. The relevant provisions are in the following Sections
 - Preferential Transactions (Sec 43 and 44)
 - Undervalued Transactions (Sec 45 to Sec 48)
 - Transactions Defrauding Creditors (Sec 49)
 - Extortionate Credit Transactions (Sec 50 and Sec 51)
 - There is also Provisions for Fraudulent Trading or wrongful Trading (Sec 66 and Sec 67)

The IRP/ RP/ Liquidator has to form an opinion, then determine the avoidance transactions and thereafter file the petition before Hon'ble NCLT under the above provisions against the perpetrators. There are timelines prescribed for the all the activities under Regulations. However the times are not mandatory as per NCLAT.

Case Law

NCLAT in the matter of *Prasant Chandra Rath (Suspended Director of Corporate Debtor) Vs. Surya Kanta Satapathy (RP) Company Appeal (AT) (Insolvency) No. 850 of 2022 and Company Appeal (AT) (Insolvency) No. 869 of 2022* in order dated 30th Sept 2022 has decided that CIRP Regulations 35-A is not mandatory and the requirement for approaching the Adjudicating Authority for appropriate relief on or before 135th day of the Insolvency Commencement Date is only directory.

Relationship between Bankruptcy, Insolvency & Liquidation

In lucid language, if any person or entity is unable to pay off the debts and it owes, to their creditor, on time or as and when they became due and payable, and if defaults then such person or entity is regarded as "insolvent".

Bankruptcy is a legal proceeding involving a person or business that is unable to repay outstanding debts. The bankruptcy process begins with a petition filed by the debtor, or by the creditors. All of the debtor's assets are measured and evaluated, and the assets may be used to repay a portion of outstanding debt.

Liquidation is the winding up of a corporation or incorporated entity. There are many persons that can initiate proceedings to cause the Liquidation, those being:-

- The Regulatory Bodies;
- The Directors of a Company;

- The Shareholders of a Company; and
- An Unpaid Creditor of a Company

In nut shell, **insolvency** is common to both bankruptcy and liquidation. Not being able to pay debts as and when they became due and payable are the leading cause of Liquidation and is the only way that can cause a natural person to become a bankrupt.

Objectives: A sound legal framework of Insolvency law was required for achieving the following objectives:-

- **Improved handling of conflicts between creditors and the debtor:** It can provide procedural certainty about the process of negotiation, in such a way as to reduce problems of common property and reduce information asymmetry for all economic participants.
- **Avoid destruction of value:** It can also provide flexibility for parties to arrive at the most efficient solution to maximise value during negotiations. The Insolvency law will create a platform for negotiation between creditors and external investors which can create the possibility of such rearrangements.
- **Drawing the line between malfeasance and business failure:**
 - (a) If malfeasance then promoters should be held responsible
 - (b) If business fails then, the company should move forward for its resolution.

The recommendations of the Bankruptcy Law Reforms Committee (BLRC) led to the enactment of the Insolvency and Bankruptcy Code, 2016 ("IBC or code") on May 28, 2016.

The IBC, consolidating all existing insolvency-related laws, has brought about a revolutionary change in the form of a robust, modern and sophisticated insolvency framework. This framework seeks to achieve a resolution for corporate debtors in distress and failing that, their liquidation in a time bound manner. Prior to the IBC, the legislative framework for insolvency and restructuring was fragmented across multiple legislations, such as the Companies Act 2013, the Sick Industrial Companies (Special Provisions) Act, 1985, Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, the Recovery of Debts due to Banks and Financial Institutions Act (RDBFI Act), 1993, the Presidency Towns Insolvency Act, 1909, the Provincial Insolvency Act, 1920.

Preamble of the Code

Objectives of the Code are given in the Preamble.

An Act to-

- Consolidate and amend the laws relating to reorganisation and insolvency resolution of corporate persons, partnership firms and individuals;
- In a time bound manner for maximisation of value of assets of such persons, - to promote entrepreneurship;

- Availability of credit;
- Balance the interests of all the stakeholders including alteration in the order of priority of payment of Government dues;
- To establish an Insolvency and Bankruptcy Board of India; and
- For matters connected therewith or incidental thereto.

IBC is not a recovery mechanism

As per preamble the objective of IBC is resolution of the corporate debtor and it cannot be used as a recovery mechanism.

Case Laws

NCLAT in the Company Appeal (AT) (Insolvency) No. 540 of 2020 dt 17th Jan 2022, in the matter of *M/s Amsons Communication Pvt. Ltd. Vs. M/s ATS Estates Pvt. Ltd.* has ordered that the provisions of Code cannot be allowed as a recovery mechanism or to recover the claim of interest by Operational Creditor.

Structure of the Code

The Code is structured into 5 parts comprising of 255 sections and 12 Schedules. Each part deals with a distinct aspect of the insolvency resolution process.

Part	Part Content	Chapters and Sections	Chapter / Contents
I	Preliminary	(1-3) Part I	1. Short title, extent & Commencement 2. Application 3. Definitions
II	Insolvency Resolutions and Liquidation for Corporate Persons	(4 – 77) Part II	1. Preliminary (Application & Definitions) 2. Corporate Insolvency Resolution Process 3. Liquidation Process 4. Pre-Packaged Insolvency Resolution Process 5. Fast Track Corporate Insolvency Resolution Process 6. Voluntary Liquidation of Corporate Persons 7. Adjudicating Authority for Corporate Persons 8. Offences & Penalties
III	Insolvency Resolution and Bankruptcy for Individuals and	(78 - 187) Part III	1. Preliminary (Application & Definitions) 2. Fresh Start Process 3. Insolvency Resolution Process 4. Bankruptcy Order for Individuals & Partnership

	Partnership Firms		Firms 5. Administration & Distribution of the Estate of the Bankrupt 6. Adjudicating Authority 7. Offences & Penalties
IV	Regulation of Insolvency Professionals, Agencies and Information Utilities	(188 – 223) Part IV	1. The Insolvency and Bankruptcy Board of India 2. Powers & Functions of the Board 3. Insolvency Professional Agencies 4. Insolvency Professionals 5. Information Utilities 6. Inspection & Investigation 7. Finance, Accounts & Audit
V	Miscellaneous	(224 – 255) Part V	Miscellaneous
	Schedules I to XII		

An **Insolvency and Bankruptcy Board of India (IBBI)** is established to administer the work of insolvency and bankruptcy of corporate persons, firms and individuals. IBBI is the regulator who regulates the main components of IBC ecosystem, i.e, Insolvency Professional Agencies (IPAs), Insolvency Professionals (IPs), Registered Valuers (RVs) and Information Utilities (IUs). IPA is the second limb of regulator.

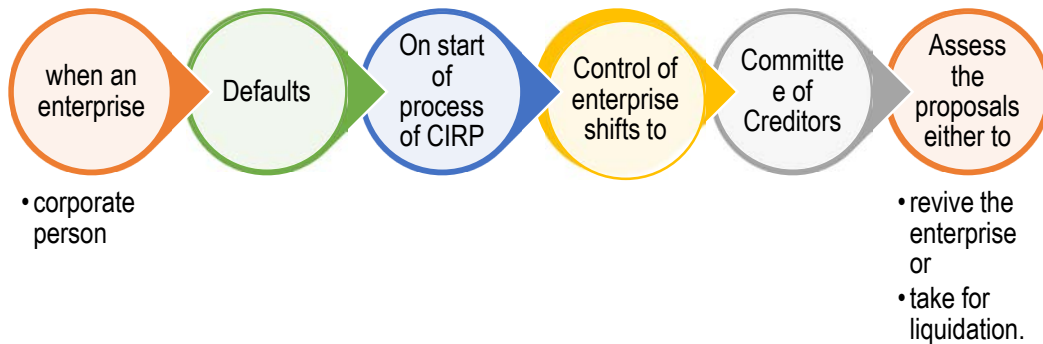
Foundation of Code

A key innovation of the IBC is a four-pillar institutional framework, comprising (a) the **first pillar**: the judicial Adjudicating Authority, being the National Company Law Tribunal (NCLT or Adjudicating Authority) where corporate insolvency matters shall be heard & NCLAT will be Appellate Authority; (b) the **second pillar**: the regulator, being Insolvency and Bankruptcy Board of India (IBBI) which has regulatory oversight over insolvency professionals and insolvency professional agencies (IPA); (c) the **third pillar**: a class of regulated persons, being the insolvency professionals who play a key role in the efficient working of the insolvency and bankruptcy process under the IBC; and, (d) the **fourth pillar**: a new industry called information utilities (IU) to electronically store facts about lenders and terms of lending.

Initiation of Corporate Insolvency Resolution Process (“CIRP”)

CIRP proceedings may be initiated against a corporate debtor by the corporate debtor itself or any of its financial creditor or operational creditor. When the Code was enacted, the minimum amount of default to initiate CIRP against a corporate debtor was INR One Lakh. However, the Central Government has by notification dated 24th March 2020 raised the threshold value of minimum amount of default to one crore rupees.

The detailed procedure for initiation of CIRP by stakeholders is described as follows:



Decisions are required to be taken in a time bound manner so that there are greater chances that the enterprise is saved as a going concern and productive resources of economy can be put to best use. The CIRP commences from the date of admission of an application filed for its initiation. The process entails a moratorium where a calm period is imposed and there is stay on suit or proceedings against the corporate debtor to give the debtor a better chance to revive and continue as a going concern. The moratorium period is 180 days and in limited circumstances, if the CoC, with a 66% majority, decides that the complexity of the case requires more time for a resolution plan to be finalized, a one-time extension of up to 90 days may be granted with prior approval of the NCLT.

The CIRP shall mandatorily be completed within a period of 330 days from the insolvency commencement date, including any extension and the time taken in legal proceedings in relation to the resolution process of the corporate debtor. The said amendment has been undertaken to ensure a timely resolution in view of the fact that the 270 day deadline was being breached on account of legal proceedings against the corporate debtor.

Provisions relating to Corporate Insolvency Resolution Process (section 4 to section 32 of the Code) will be applicable.

Provisions relating to Liquidation Process of Corporates (section 33 to section 54 of the Code) will be applicable in case where the enterprise is undergoing liquidation.

Provisions relating to Fast Track Corporate Insolvency Resolution Process of Small Corporate Persons (section 55 to section 58 of Insolvency Code) will be applicable in case where the enterprise is a small company as per Companies Act, 2013 or a start-up or an unlisted company with total assets not exceeding rupees one crore.

Provisions relating to Voluntary Liquidation (section 59 of the Code) will be applicable to corporate person who intends to liquidate itself voluntarily and has not committed any default.

Winding up of companies - In most of the cases, winding up of companies will be through the Liquidation Process under the Code only.

Bankruptcy of individuals and firms - Part III of Insolvency Code 2016 (containing sections 78-187) deals with insolvency resolution and bankruptcy for individuals and partnership firms. This Part shall apply to matters relating to fresh start, insolvency and bankruptcy of individuals and partnership firms. Debt Recovery Tribunal (DRT) will be the Adjudicating Authority and Debt Recovery Appellate Tribunal (DRAT) will be the Appellate Authority for individuals and firms. These provisions are not yet effective except for the provisions pertaining to personal guarantors to corporate debtors in which case the NCLT will be the Adjudicating Authority and NCLAT will be Appellate Authority, if the process is going on or otherwise DRT/ DRAT.

Flow of insolvency resolution process for individuals-

- The process will be managed by 'resolution professional' under the direction of 'Adjudicating Authority'.
- Insolvency Resolution Process will be initiated.
- Finalise 'repayment plan' with concurrence of debtor and committee of creditors.
- Upon consensus on repayment plan the individual or firm will get a discharge order.
- On failure to finalize the repayment plan, the creditors/debtor can file an application for 'bankruptcy' and the Adjudicating Authority may pass the bankruptcy order.
- The resolution professional who is a bankruptcy trustee will take over estate of the bankrupt. He will sell or dispose it off and satisfy payments of creditors to the extent possible.
- After that, the bankrupt will get a 'discharge order'.
- The discharge order will be registered with Board (IBBI) in a register referred to in section 196 of the Code.

Provisions of this Code to override other laws: Section 238 of the Code states that the Code shall have overriding effect over other laws.

For example, sections 53 and 178 of Insolvency and Bankruptcy Code, 2016 provide that distribution from sale of assets will be as specified in that section, notwithstanding anything to the contrary contained in any other law enacted by the Parliament or any State Legislature for the time being in force.

Many tax laws (including GST) also provide for first charge on assets of the taxable person. However, with the overriding effect of Section 238, distribution from sale of assets in Liquidation Process or payment as per the resolution plan in CIRP under the Code, will prevail over other laws.

Extent and Commencement of the Code:

As per section 1 of the Insolvency and Bankruptcy Code, it extends to the whole of India.

This Code came into enforcement on 28th May 2016, however, the Central Government appointed different dates for different provisions of this Code.

Significant amendments: The Code has been first amended by the Insolvency and Bankruptcy (Amendment) Ordinance, 2017, passed on November 23, 2017. This Ordinance became an Act on January 18, 2018. It was known as the Insolvency and Bankruptcy Code (Amendment) Act, 2018. It was made applicable from November 23, 2017.

The second amendment was made vide the **Insolvency and Bankruptcy Code (Amendment) Ordinance, 2018, on June 6, 2018**. Further, the said ordinance, in the form of the Insolvency and Bankruptcy (Second Amendment) Bill received the assent of the President on the 17th August, 2018 and thus the **Insolvency and Bankruptcy Code (Second Amendment) Act, 2018** was enacted.

The third amendment was made vide the **Insolvency and Bankruptcy Code (Amendment) Bill, 2019** which received the assent of the President on 5th August, 2019 and thus the **Insolvency and Bankruptcy Code (Amendment) Act, 2019** was promulgated.

The fourth amendment was made vide the **Insolvency and Bankruptcy Code (Amendment) Ordinance, 2019, on December 28, 2019**. Further, the said ordinance, in the form of the Insolvency and Bankruptcy (Amendment) Bill, 2020 received the assent of the President on the 13th March, 2020 and thus the **Insolvency and Bankruptcy Code (Amendment) Act, 2020** was enacted.

Due to the advent of COVID-19 pandemic, the IBC was amended by insertion of Section 10A to suspend the initiation of CIRP under Sections 7, 9 and 10 of the IBC for any default arising on or after March 25, 2020.

The Code has undergone significant amendments since its enactment-

- to keep up with the developments and demands of the economy
- for effective implementation of law
- to remove the bottlenecks

To achieve desired objectives of the Code, the President promulgated the 'Insolvency and Bankruptcy Code (Amendment) Ordinance, 2021 on 4th April 2021. The Ministry of Law and Justice on 12th of August 2021 enacted the Insolvency and Bankruptcy Code (Amendment) Act, 2021 w.r.e.f from 4th day of April, 2021.

The amendments was made with an intent to provide an efficient alternative insolvency resolution framework for corporate persons classified as micro, small and medium enterprises (MSMEs) under the Code, for ensuring quicker, cost-effective and value maximizing outcomes for all the stakeholders, in a manner which is least disruptive to the continuity of MSMEs businesses and which preserves jobs. By this amendment the Provisions related to PPIRP and MSMEs was introduced.

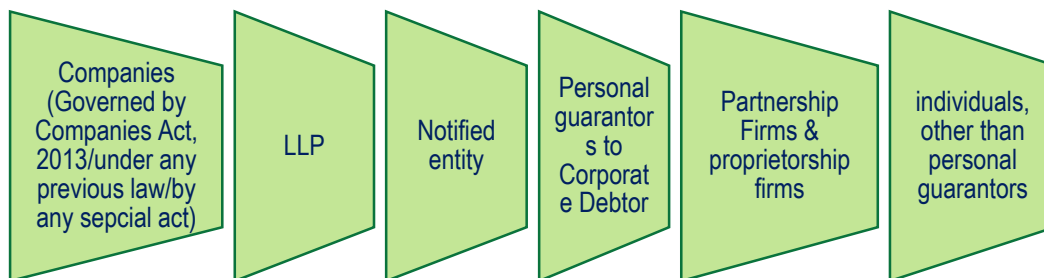
It provides an efficient alternative insolvency resolution framework for corporate persons classified as MSMEs for timely, efficient & cost-effective resolution of distress thereby ensuring positive signal to debt market, employment preservation, ease of doing business and preservation of enterprise

capital. Other expected impact and benefits of the amendment in Code are lesser burden on Adjudicating Authority, assured continuity of business operations for corporate debtor (CD), less process costs & maximum assets realization for financial creditors (FC) and assurance of continued business relation with CD and rights protection for operational Creditors (OC).

Applicability of the Code [Section 2]

The provisions of the Code shall apply for insolvency, liquidation, voluntary liquidation or bankruptcy of the following entities:-

- (a) Any company incorporated under the Companies Act, 2013 or under any previous law.
- (b) Any other company governed by any special act for the time being in force, except in so far as the said provision is inconsistent with the provisions of such Special Act.
- (c) Any Limited Liability Partnership under the LLP Act 2008.
- (d) Any other body incorporated under any law for the time being in force, as the Central Government may by notification specify in this behalf.
- (e) ²Personal guarantors to corporate debtors (CD);
- (f) Partnership firms and proprietorship firms; and
- (g) Individuals, other than persons referred to in clause (e)



Case Law

SC in *Lalit Kumar Jain v. Union of India*, in 2021 held with respect to the “Application of Code” that there is sufficient indication in Code by sections 2(e), 5(22), sections 60 and 179 indicating that personal guarantors, though forming part of larger grouping of individuals, are to be, in view of their intrinsic connection with corporate debtors, dealt with differently, through same adjudicatory process and by same forum as such corporate debtors.

² Personal guarantors of corporate debtors have been treated as a separate class. The application for bankruptcy of individual personal guarantor will have to be filed before NCLT as per section 60(2) of the IBC, 2016. Insolvency Code has been made applicable to personal guarantors of corporates w.e.f. 23-11-2017

Notification No. S.O. 4126 (E), dated 15-11-2019 making provisions of IBC applicable in respect of 'personal guarantors to corporate debtors' as another category of persons is valid. Even the approval of a resolution plan does not ipso facto discharge a personal guarantor (of a corporate debtor) of her or his liabilities under contract of guarantee.

Non-applicability of the Code: The Code is not applicable to corporates in finance sector. Section 3(7) of Insolvency & Bankruptcy Code, 2016 states that "Corporate person" shall not include any financial service provider.

"Financial service provider" means a person engaged in the business of providing financial services in terms of authorisation issued or registration granted by a financial sector regulator [section 3(17)].

However, section 227 of the Code, which was notified on 1-5-2018 provided that, Central Government can notify financial service providers for purpose of insolvency and liquidation proceedings, which may be conducted under the Insolvency & Bankruptcy Code, in consultation with appropriate financial sector regulator. As per notification dated 18-11-2019 it has been notified by the central government that insolvency resolution and liquidation proceedings of non-banking finance companies (which include housing finance companies) with asset size of Rs.500 crore or more, as per last audited balance sheet, shall be undertaken in accordance with the provisions of the Code and Rules made thereunder.

Case Laws

National Company Law Tribunal, Mumbai Bench, in 2022 decided in the *State Co-operative Bank Ltd. v. Shri Siddheshwar Sahakari Sakhar Karkhana Ltd.* that corporate debtor being a co-operative society was not a corporate person to whom provision of Code were applicable. Here as corporate debtor was registered/incorporated under Multi-State Co-operative Societies Act, 2002, which provides specific statutes for winding up of societies registered under same, and hence corporate debtor could not be put under insolvency resolution process.



2. IMPORTANT DEFINITIONS [SECTIONS 3 AND 5]

- (1) **Board** means the Insolvency and Bankruptcy Board of India (IBBI) established under section 188(1) of the Code [Section 3(1)].

The Board shall be a body corporate by the name aforesaid, having perpetual succession and a common seal, with power, subject to the provisions of this Code, to acquire, hold and dispose of property, both movable and immovable, and to contract, and shall, by the said name, sue or be sued [Section 188(2)].

The board will have powers of civil court as to the issue of summons, discovery and production of books, inspection of books/registers and issue of commissions for examination of witnesses [Section 196(3) of the Code]

- (2) **Charge** means an interest or lien created on the property or assets of any person or any of its undertakings or both, as the case may be, as security and includes a mortgage; [Section 3(4)]
- (3) **Claim** means:
- (a) **a right to payment**, whether or not such right is reduced to judgment, fixed, disputed, undisputed, legal, equitable, secured, or unsecured;
 - (b) **right to remedy for breach of contract** under any law for the time being in force, if such breach gives rise to a right to payment, whether or not such right is reduced to judgment, fixed, matured, unmatured, disputed, undisputed, secured or unsecured; [Section 3(6)]
- (4) **Corporate Person** means :
- (a) a company as defined under section 2(20) of the Companies Act, 2013;
 - (b) a Limited Liability Partnership as defined in 2(1)(n) of Limited Liability Act, 2008; or,
 - (c) any other person incorporated with limited liability under any law for the time being in force but shall not include any financial service provider. [Section 3(7)]
- (5) **Corporate Debtor** means a corporate person who owes a debt to any person. [Section 3(8)]
- (6) **Creditor** means any person to whom a debt is owed and includes –
- a financial creditor,
 - an operational creditor,
 - a secured creditor,
 - an unsecured creditor, and
 - a decree holder. [Section 3(10)]
- (7) **Debt** means a liability or obligation in respect of a claim which is due from any person and includes a financial debt and operational debt. [Section 3(11)]

Financial Debt - "Financial debt" means a debt along with interest, if any, which is disbursed against the consideration for the time value of money and includes—

- (a) money borrowed against the payment of interest.
- (b) any amount raised by acceptance under any acceptance credit facility or its dematerialised equivalent.
- (c) any amount raised pursuant to any note purchase facility or the issue of bonds, notes, debentures, loan stock or any similar instrument.

- (d) the amount of any liability in respect of any lease or hire purchase contract which is deemed as a finance or capital lease under the Indian Accounting Standards or such other accounting standards as may be prescribed.
- (e) receivables sold or discounted other than any receivables sold on non-recourse basis.
- (f) any amount raised under any other transaction, including any forward sale or purchase agreement, having the commercial effect of a borrowing.

Explanation.— For the purposes of this sub-clause - (i) any amount raised from an allottee under a real estate project shall be deemed to be an amount having the commercial effect of a borrowing; and (ii) the expressions, "allottee" and "real estate project" shall have the meanings respectively assigned to them in section 2(d) and 2(zn) of the Real Estate (Regulation and Development) Act, 2016 .

- (g) any derivative transaction entered into in connection with protection against or benefit from fluctuation in any rate or price and for calculating the value of any derivative transaction, only the market value of such transaction shall be taken into account.
- (h) any counter-indemnity obligation in respect of a guarantee, indemnity, bond, documentary letter of credit or any other instrument issued by a bank or financial institution.
- (i) the amount of any liability in respect of any of the guarantee or indemnity for any of the items referred to in sub-clauses (a) to (h) of this clause [Section 5(8) of Code, 2016]

Subscription money for purchase of shares is not financial debt - Subscription money for purchase of shares is not financial debt - *ACPC Enterprises v. Affinity Beauty Saloon (2018)* (NCLT – Delhi Bench)

Operational debt as per section 5(21) of the Code means a claim in respect of the provision of goods or services including employment or a debt in respect of the payment of dues arising under any law for the time being in force and payable to the Central Government, any State Government or any local authority;

- (8) **Default** means non-payment of debt when whole or any part or instalment of the amount of debt has become due and payable and is not paid by the debtor or the corporate debtor, as the case may be. [Section 3(12)]
- (9) **Financial service** includes any of the following services, namely:—
 - (a) accepting of deposits;
 - (b) safeguarding and administering assets consisting of financial products, belonging to another person, or agreeing to do so;
 - (c) effecting contracts of insurance;

- (d) offering, managing or agreeing to manage assets consisting of financial products belonging to another person;
- (e) rendering or agreeing, for consideration, to render advice on or soliciting for the purposes of—
 - (i) buying, selling, or subscribing to, a financial product;
 - (ii) availing a financial service; or
 - (iii) exercising any right associated with a financial product or financial service;
- (f) establishing or operating an investment scheme;
- (g) maintaining or transferring records of ownership of a financial product;
- (h) underwriting the issuance or subscription of a financial product; or
- (i) selling, providing, or issuing stored value or payment instruments or providing payment services; [Section 3(16)]

- (10) **Financial Service Provider** means a person engaged in the business of providing financial services in terms of authorisation issued or registration granted by a financial sector regulator [Section 3(17)]

Financial Service Providers include banks, financial institutions, insurance companies, mutual funds etc.

- (11) **Financial Sector Regulator** means an authority or body constituted under any law for the time being in force to regulate services or transactions of financial sector and includes-

- the Reserve Bank of India,
- the Securities and Exchange Board of India,
- the Insurance Regulatory and Development Authority of India,
- the Pension Fund Regulatory Authority, and
- such other regulatory authorities as may be notified by the Central Government; [Section 3(18)]

- (12) **Insolvency professional (IP)** means a person enrolled under section 206 with an insolvency professional agency as its member and registered with the Board as an insolvency professional under section 207; [Section 3(19)]

Insolvency Professional is required to play a key role in implementation of the Code.

The word 'person', used refers to an individual to be IP. A LLP, partnership firm or a company can only be recognized as 'Insolvency Professional Entity' (IPE), which is not defined under the Code.

The Insolvency Professional should follow code of conduct as specified in section 208(2) of Insolvency Code and in First Schedule to Insolvency and Bankruptcy Board of India (Insolvency Professionals) Regulations, 2016.

- (13) **"Insolvency professional agency"** means any person registered with the Board under section 201 as an insolvency professional agency; [Section 3(20)]

Work relating to insolvency resolution is expected to be handled by 'Insolvency Professionals' (IP). These professionals are required to be registered with 'Insolvency Professional Agency' (IPA).

The Insolvency Professional Agencies (IPA) will develop professional standards, code of ethics and be first level regulator for insolvency professionals members. This will lead to development of a competitive industry for such professionals.

- (14) **"Information utility"** means a person who is registered with the Board as an information utility under section 210; [Section 3(21)]

The Insolvency and Bankruptcy processes are expected to function on basis of financial information available electronically.

Information Utility will collect, collate, authenticate and disseminate financial information to be used in insolvency, liquidation and bankruptcy proceedings.

- (15) A **person** includes:-

- an individual
- a Hindu Undivided Family
- a company
- a trust
- a partnership
- A limited liability partnership, and
- any other entity established under a Statute.

And includes a person resident outside India [Section 3(23)]

"Person resident outside India" means a person other than a person resident in India [section 3(25)].

"Person resident in India" shall have the meaning as assigned to such term in section 2(v) of FEMA [Section 3(24)]

- (16) **Property** includes money, goods, actionable claims, land and every description of property situated in India or outside India and every description of interest including present or future or vested or contingent interest arising out of, or incidental to, property; [Section 3(27)]

- (17) **Secured creditor** means a creditor in favour of whom security interest is created; [Section 3(30)]
- (18) **Security Interest** means right, title or interest or a claim to property, created in favour of, or provided for a secured creditor by a transaction which secures payment or performance of an obligation and includes mortgage, charge, hypothecation, assignment and encumbrance or any other agreement or arrangement securing payment or performance of any obligation of any person. [Section 3(31)]
- (19) A **transaction** includes an agreement or arrangement in writing for transfer of assets, or funds, goods or services, from or to the corporate debtor. [Section 3(33)]
- (20) **Transfer** includes sale, purchase, exchange, mortgage, pledge, gift, loan or any other form of transfer of right, title, possession or lien. [Section 3(34)]
- (21) **Adjudicating Authority-** National Company Law Tribunal (NCLT) constituted under section 408 of the Companies Act, 2013 is the Adjudicating Authority (AA) for purpose of insolvency resolution and liquidation for corporate persons and personal guarantors thereof [section 5(1) read with section 60(1) of the Code]

NCLT is also AA for the insolvency resolution or liquidation or bankruptcy of the corporate guarantor or personal guarantor of such CD when insolvency resolution or liquidation of such CD is pending before AA. [Section 60(2) of the Code]

National Company Law Appellate Tribunal (NCLAT) is the appellate authority over decisions of NCLT [section 61 of the Code]

Appeal against order of NCLAT can be filed to Supreme Court on question of law arising out of such order, within 45 days [section 62 of the Code]

Debt Recovery Tribunal (DRT) will be adjudicating authority for individuals and firms subject to section 60(2) – [section 179(1) of the Code]

- (22) **"Base resolution plan"** means a resolution plan provided by the corporate debtor under clause (c) of sub-section (4) of section 54A, which deals with the Corporate debtors eligible for pre-packaged insolvency resolution process; [Section 5(2A)]
- (23) **Corporate applicant means—**

- (a) corporate debtor; or
- (b) a member or partner of the corporate debtor who is authorised to make an application for the corporate insolvency resolution process or the pre-packaged insolvency resolution process, as the case may, under the constitutional document of the corporate debtor; or
- (c) an individual who is in charge of managing the operations and resources of the corporate debtor; or

- (d) a person who has the control and supervision over the financial affairs of the corporate debtor; [Section 5(5)]
- (24) **Corporate guarantor** means a corporate person who is the surety in a contract of guarantee to a corporate debtor; [Section 5(5A)]
- (25) **Dispute** includes a suit or arbitration proceedings relating to—
- the existence of the amount of debt;
 - the quality of goods or service; or
 - the breach of a representation or warranty; [Section 5(6)]
- (26) **Financial creditor** means any person to whom a financial debt is owed and includes a person to whom such debt has been legally assigned or transferred to; [section 5(7)]
- (27) **Financial Debt** means a debt along with interest, if any, which is disbursed against the consideration for the time value of money and includes—
- money borrowed against the payment of interest;
 - any amount raised by acceptance under any acceptance credit facility or its dematerialised equivalent;
 - any amount raised pursuant to any note purchase facility or the issue of bonds, notes, debentures, loan stock or any similar instrument;
 - the amount of any liability in respect of any lease or hire purchase contract which is deemed as a finance or capital lease under the Indian Accounting Standards or such other accounting standards as may be prescribed;
 - receivables sold or discounted other than any receivables sold on non-recourse basis;
 - any amount raised under any other transaction, including any forward sale or purchase agreement, having the commercial effect of a borrowing;

Explanation -For the purposes of this sub-clause -

- any amount raised from an allottee under a real estate project shall be deemed to be an amount having the commercial effect of a borrowing; and
 - the expressions, “allottee” and “real estate project” shall have the meanings respectively assigned to them in clauses (d) and (zn) of section 2 of the Real Estate (Regulation and Development) Act, 2016;
- (g) any derivative transaction entered into in connection with protection against or benefit from fluctuation in any rate or price and for calculating the value of any derivative transaction, only the market value of such transaction shall be taken into account;

- (h) any counter-indemnity obligation in respect of a guarantee, indemnity, bond, documentary letter of credit or any other instrument issued by a bank or financial institution;
- (i) the amount of any liability in respect of any of the guarantee or indemnity for any of the items referred to in sub-clause (a) to (h) of this clause; [Section 5(8)]
- (28) **Initiation date** means the date on which a financial creditor, corporate applicant or operational creditor, as the case may be, makes an application to the Adjudicating Authority for initiating corporate insolvency resolution process or pre-packaged insolvency resolution process, as the case may be; [Section 5(11)]
- (29) **Insolvency commencement date** means the date of admission of an application for initiating corporate insolvency resolution process by the Adjudicating Authority under sections 7, 9 or section 10, as the case may be; [Section 5(12)]
- (30) **Insolvency resolution process period** means the period of one hundred and eighty days beginning from the insolvency commencement date and ending on one hundred and eightieth day; [Section 5(14)]
- (31) **Liquidation commencement date** means the date on which proceedings for liquidation commence in accordance with section 33 (Initiation of Liquidation) or section 59 (Voluntary Liquidation of corporate persons), as the case may be; [Section 5(17)]
- (32) **Liquidator** means an insolvency professional appointed as a liquidator in accordance with the provisions of Chapter III or Chapter V of this Part, as the case may be;
- (33) **Operational creditor** means a person to whom an operational debt is owed and includes any person to whom such debt has been legally assigned or transferred; [Section 5(20)]
- (34) **Personal guarantor** means an individual who is the surety in a contract of guarantee to a corporate debtor; [Section 5(22)]
- (35) **Related party, in relation to a corporate debtor, means—**
 - (a) **a director or partner or a relative** of a director or partner of the corporate debtor
 - (b) **a key managerial personnel or a relative** of a key managerial personnel of the corporate debtor;
 - (c) **a limited liability partnership or a partnership firm** in which a director, partner, or manager of the corporate debtor or his relative is a partner;
 - (d) **a private company** in which a director, partner or manager of the corporate debtor is a director and holds along with his relatives, more than two per cent. of its share capital;
 - (e) **a public company** in which a director, partner or manager of the corporate debtor is a director and holds along with relatives, more than two per cent. of its paid-up share capital;

- (f) **any body corporate** whose board of directors, managing director or manager, in the ordinary course of business, acts on the advice, directions or instructions of a director, partner or manager of the corporate debtor;
 - (g) **any limited liability partnership or a partnership firm** whose partners or employees in the ordinary course of business, acts on the advice, directions or instructions of a director, partner or manager of the corporate debtor;
 - (h) **any person** on whose advice, directions or instructions, a director, partner or manager of the corporate debtor is accustomed to act;
 - (i) **a body corporate which is a holding, subsidiary or an associate company** of the corporate debtor, or a subsidiary of a holding company to which the corporate debtor is a subsidiary;
 - (j) **any person who controls** more than twenty per cent. of voting rights in the corporate debtor on account of ownership or a voting agreement;
 - (k) **any person in whom the corporate debtor controls** more than twenty per cent. of voting rights on account of ownership or a voting agreement;
 - (l) **any person who can control the composition** of the board of directors or corresponding governing body of the corporate debtor;
 - (m) **any person who is associated with the corporate debtor** on account of—
 - (i) participation in policy making processes of the corporate debtor; or
 - (ii) having more than two directors in common between the corporate debtor and such person; or
 - (iii) interchange of managerial personnel between the corporate debtor and such person;
 - (iv) provision of essential technical information to, or from, the corporate debtor; [Section 5(24)]
- (36) **"related party", in relation to an individual**, means—
- (a) a person who is a relative of the individual or a relative of the spouse of the individual;
 - (b) a partner of a limited liability partnership, or a limited liability partnership or a partnership firm, in which the individual is a partner;
 - (c) a person who is a trustee of a trust in which the beneficiary of the trust includes the individual, or the terms of the trust confers a power on the trustee which may be exercised for the benefit of the individual;

- (d) a private company in which the individual is a director and holds along with his relatives, more than two per cent of its share capital;
- (e) a public company in which the individual is a director and holds along with relatives, more than two per cent of its paid-up share capital;
- (f) a body corporate whose board of directors, managing director or manager, in the ordinary course of business, acts on the advice, directions or instructions of the individual;
- (g) a limited liability partnership or a partnership firm whose partners or employees in the ordinary course of business, act on the advice, directions or instructions of the individual;
- (h) a person on whose advice, directions or instructions, the individual is accustomed to act;
- (i) a company, where the individual or the individual along with its related party, own more than fifty per cent of the share capital of the company or controls the appointment of the board of directors of the company.

Explanation.—For the purposes of this clause,—

- (a) "relative", with reference to any person, means anyone who is related to another, in the following manner, namely:—
 - (i) members of a Hindu Undivided Family,
 - (ii) husband,
 - (iii) wife,
 - (iv) father,
 - (v) mother,
 - (vi) son,
 - (vii) daughter,
 - (viii) son's daughter and son,
 - (ix) daughter's daughter and son,
 - (x) grandson's daughter and son,
 - (xi) granddaughter's daughter and son,
 - (xii) brother,
 - (xiii) sister,
 - (xiv) brother's son and daughter,
 - (xv) sister's son and daughter,
 - (xvi) father's father and mother,
 - (xvii) mother's father and mother,

- (xviii) father's brother and sister,
 - (xix) mother's brother and sister, and
 - (b) wherever the relation is that of a son, daughter, sister or brother, their spouses shall also be included; [Section 5(24A)]
- (37) **"Resolution applicant"** means a person, who individually or jointly with any other person, submits a resolution plan to the resolution professional pursuant to the invitation made under section 25(2)(h) or pursuant to section 54K, as the case may be [Section 5(25)]
- (38) **"Resolution plan"** means a plan proposed by resolution applicant for insolvency resolution of the corporate debtor as a going concern in accordance with Part II; [Section 5(26)]
- Explanation.- For removal of doubts, it is hereby clarified that a resolution plan may include provisions for the restructuring of the corporate debtor, including by way of merger, amalgamation and demerger
- (39) **Resolution professional**, for the purposes of this Part, means an insolvency professional appointed to conduct the corporate insolvency resolution process or the pre-packaged insolvency resolution process, as the case may be, and includes an interim resolution professional; [Section 5(27)]
- (40) **Voting share** means the share of the voting rights of a single financial creditor in the committee of creditors which is based on the proportion of the financial debt owed to such financial creditor in relation to the financial debt owed by the corporate debtor. [Section 5(28)]



3. CORPORATE INSOLVENCY RESOLUTION PROCESS [SECTIONS 4, 6-32 AND 32A]

Provisions related to Insolvency Resolution and Liquidation process for Corporate Persons are covered in Part II of the Code. This part comprises of seven chapters with section 4 to 77 of the Code. Each chapter deals with different issues relating to Insolvency Resolution and Liquidation of Corporate Persons.

Corporate Insolvency Resolution Process (CIRP) is a process during which the Committee of Creditors (CoC) assess whether the debtor's business is feasible and viable to continue, the options for its rescue and revival, if any and endeavour is to keep it as a going concern. If the insolvency resolution process fails or CoC decide that the business of debtor cannot be revived then, the debtor will undergo liquidation process and the assets of the debtor shall be realized and distributed by the liquidator among the stakeholders as per Sec 53. The liquidation can also be on a going concern basis where the corporate debtor shall not be dissolved.

The Insolvency Resolution Process provides a collective mechanism to lenders to deal with the overall distressed position of a corporate debtor. This is a significant departure from the earlier legal

framework under which the primary onus to initiate a re-organization process lies with the debtor, and lenders may pursue distinct actions for recovery, security enforcement and debt restructuring.

The Code creates time-bound processes for insolvency resolution of companies and individuals. These processes is to be completed within 180 days, extendable by 90 days, however the overall process has to be completed within an outer time limit of 330 days. However, in certain exceptional cases, it may be open for the Adjudicating Authority and/or Appellate Tribunal to extend the time beyond 330 days³.

The Code also provides for fast-track resolution of corporate insolvency within 90 days. If insolvency cannot be resolved, the assets of the borrowers may be sold to repay creditors.

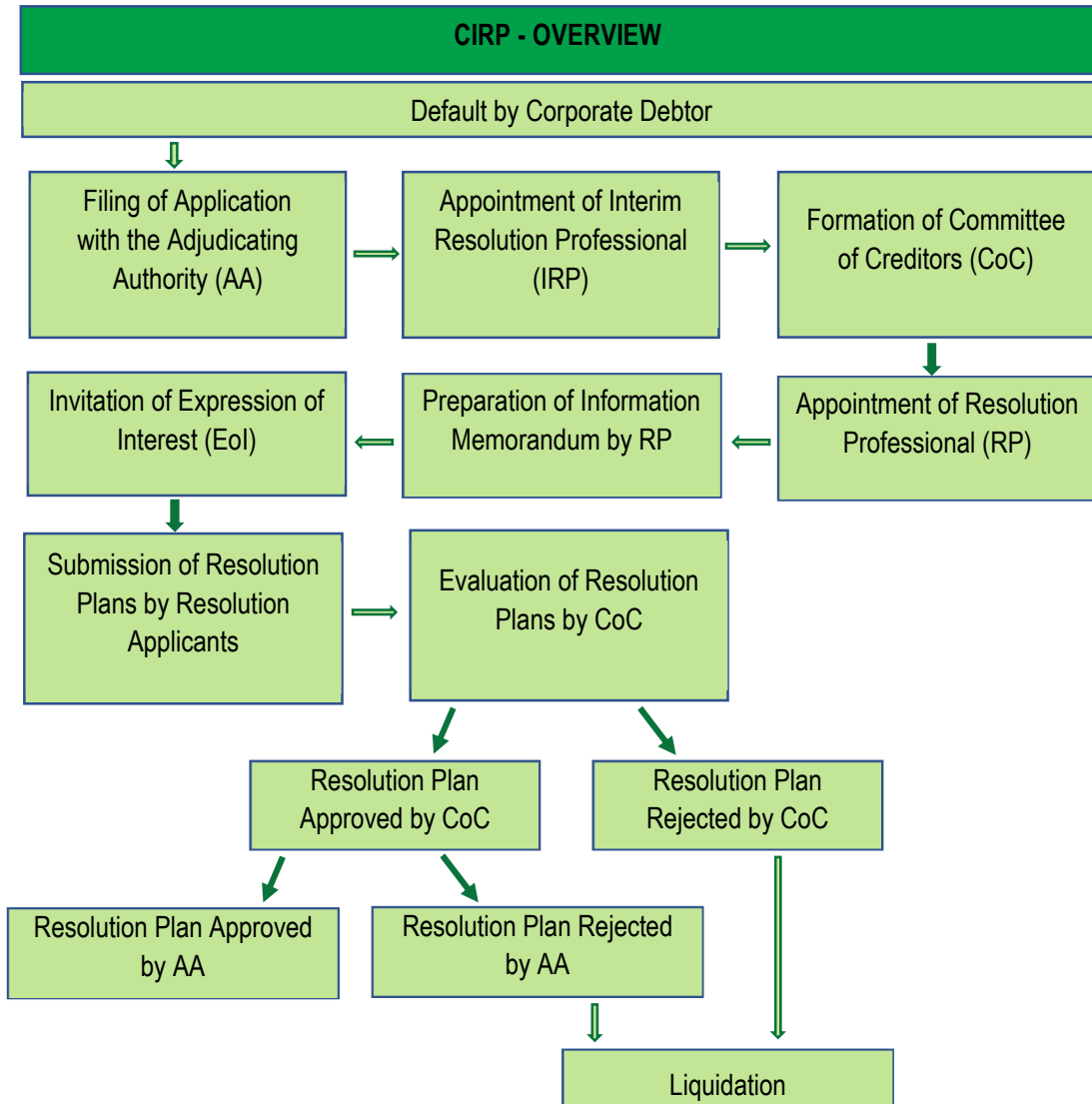
Process Flow

A comprehensive process that covers the gamut of insolvency resolution framework for Corporates and includes processes relating to:-

- Filing of application before NCLT by a financial creditor, operational creditor or a corporate applicant;
- Adjudication: Admission or Rejection of application. If admitted then:
 - Moratorium and Public Announcement;
 - Appointment of Interim Resolution Professional ;
 - Calling of claims ;
 - Formation of the Committee of Creditors
 - Appointment of Resolution Professional
 - Taking control and managing the operations of the corporate debtor by the IRP/ RP
 - Appointment of Registered Valuers
 - Preparation of Information memorandum & Invitation for Expression of Interest
 - Submission of Expression of Interest by prospective resolution applicants
 - Preparation of provisional and final list of resolution applicants by the Resolution Professional.
 - Issue of Request for Resolution Plan (RFRP), Information Memorandum and Evaluation Matrix to all the prospective resolution applicants
 - Submission of Resolution Plan by resolution applicants
 - Approval or rejection of the Resolution Plan by the CoC

³ CoC of Essar Steel India Limited vs. Satish Kumar Gupta & Ors. (Civil Appeal No. 8766-67 of 2019)

- Approval or rejection of the Resolution Plan by the NCLT (Adjudicating Authority)
- Implementation of Resolution Plan if approved by NCLT



(I) Application to National Company Law Tribunal

The process of insolvency is triggered by occurrence of default. As per Section 3 (12) of the Code, **default** means non-payment of debt when whole or any part or installment of the amount of debt has become due and payable and is not paid by the debtor or the corporate debtor.

The provisions relating to the insolvency and liquidation of corporate debtors shall be applicable only when the amount of the default is one lakh rupees or more. However, the Central Government has

by notification dated 24th March 2020 raised the threshold value of minimum amount of default to one crore rupees (section 4).

Provided further that the Central Government may, by notification, specify such minimum amount of default of higher value, which shall not be more than one crore rupees, for matters relating to the pre-packaged insolvency resolution process of corporate debtors under Chapter III-A.

Filing of application before NCLT

The corporate insolvency process may be initiated against any defaulting corporate debtor by making an application for corporate insolvency resolution process before NCLT.

(II) Who can initiate insolvency resolution process?

Where any corporate debtor commits a default, a financial creditor, an operational creditor or the corporate debtor itself may initiate corporate insolvency resolution process in respect of such corporate debtor in the manner as provided under this Chapter (Chapter II of part II) [Section 6].

Provisions and procedures relating to each initiator are different.

Accordingly, the application may be made by:-

Financial creditor any person to whom a financial debt is owed &

- Includes a person to whom such debt is legally assigned or transferred;

Operational creditor any person to whom a operational debt is owed &

- Includes a person to whom such debt is legally assigned or transferred ;

Corporate debtor A corporate person who owes a debt to any person and committed default.

(A) Initiation of corporate insolvency resolution process by financial creditor

- (1) **Filing of application before adjudicating authority:** A financial creditor either by itself or jointly with other financial creditors, or any other person on behalf of the financial creditor, as may be notified by the Central Government, may file an application for initiating corporate insolvency resolution process against a corporate debtor before the Adjudicating Authority when a default has occurred.

Provided that for the financial creditors, **referred to in clauses (a) and (b) of sub-section (6A) of section 21**, an application for initiating corporate insolvency resolution process against the corporate debtor **shall be filed jointly** by not less than one hundred of such creditors in the same class or not less than ten per cent, of the total number of such creditors in the same class, whichever is less:

Provided further that for **financial creditors who are allottees** under a real estate project, an application for initiating corporate insolvency resolution process against the corporate

debtor **shall be filed jointly** by not less than one hundred of such allottees under the same real estate project or not less than ten per cent, of the total number of such allottees under the same real estate project, whichever is less:

Explanation: For the purposes of this sub-section, a default includes a default in respect of a financial debt owed not only to the applicant financial creditor but to any other financial creditor of the corporate debtor.

Vide Notification S.O.1091(E) dated 27th February, 2019, the Central government hereby notified following persons who may file an application for initiating corporate insolvency resolution process against a corporate debtor before the Adjudicating Authority, on behalf of the Financial Creditor:-

- (i) a guardian;
 - (ii) an executor or administrator of an estate of a financial creditor;
 - (iii) a trustee (including a debenture trustee); and
 - (iv) a person duly authorized by the Board of Directors of a Company.
- (2) **Procedure to be followed by the Financial creditor:** The financial creditor shall file an application by itself / jointly against a corporate debtor before NCLT in accordance with the provisions contained in Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016, Copy of such an application shall be forwarded to registered office of corporate debtor and to the Board, by registered post or speed post or by hand or by electronic means, before filing with the Adjudicating Authority .

Financial creditor shall along with the application furnish—

- (a) **record of the default** recorded with the information utility or such other record or evidence of default as may be specified;
 - (b) **the name of the insolvency professional** proposed to act as an interim resolution professional; and
 - (c) **any other information** as may be specified by the Board.
- (3) **Time period for determination of default:** The Adjudicating Authority shall, within fourteen days of the receipt of the application, ascertain the existence of a default from the records of an information utility or on the basis of other evidence furnished by the financial creditor.

Provided that if the Adjudicating Authority has not ascertained the existence of default and passed an order within such time as specified, it shall record its reasons in writing for the same.

Case Law

Supreme Court in *Surendra Trading Company Vs. Juggilal Kamlatpat Jute Mills Company Ltd. & Others* prescribed time period for determination of defaults. It was held that the time limit prescribed in IBC, 2016 for admitting or rejecting a petition or initiation of CIRP under proviso to sub-section (5) of section 7 or sub-section (5) of section 9 or sub-section (4) of section 10 is procedural in nature, a tool of aid in expeditious dispensation of justice and is directory.

Various provisions of the Code would indicate that there are three stages:

(i) First stage: Filing of the application: When the application is filed, the Registry of the Adjudicating Authority is supposed to scrutinize the same to find out as to whether it is complete in all respects or there are certain defects. If it is complete, the same shall be posted for preliminary hearing before the Adjudicating Authority.

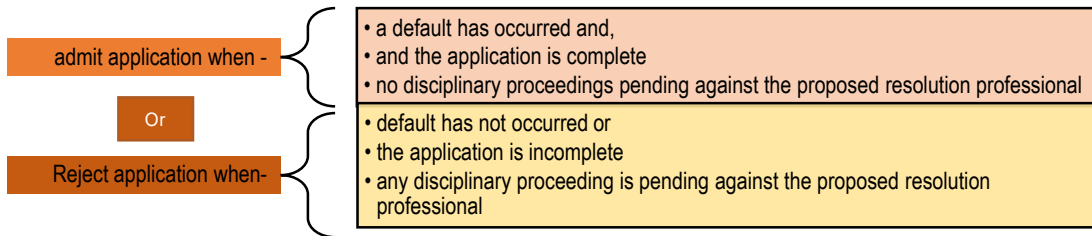
If there are defects, the applicant would be notified about those defects so that these are removed. For this purpose, seven days' time is given. Once the defects are removed then the application would be posted before the Adjudicating Authority.

(ii) Second Stage: When the application is listed before the Adjudicating Authority: It has to take a decision to either admit or reject the application. For this purpose, fourteen days' time is granted to the Adjudicating Authority. If the application is rejected, the matter is given a *quietus* (i.e. dead) at that level itself. However, if it is admitted, we enter the third stage.

(iii) Third Stage: After admission of the application: As application is admitted, insolvency resolution process commences. This resolution process is to be completed within 180 days, which is extendable, in certain cases, up to 90 days. Insofar as the first stage is concerned, it has no bearing on the insolvency resolution process at all, inasmuch as, unless the application is complete in every respect, the Adjudicating Authority is not supposed to deal with the same. It is at the second stage that the Adjudicating Authority is to apply its mind and decide as to whether the application should be admitted or rejected. Here adjudication process starts. However, in spite thereof, when this period of fourteen days given by the statute to the Adjudicating Authority to take a decision to admit or reject the application is directory, there is no reason to make it mandatory in respect of the first stage, which is pre-adjudication stage.

Thus, provision of removing the defects within seven days is directory and not mandatory in nature.

- (4) **Order:** Where the Adjudicating Authority is satisfied, it may either —



Notice to rectify the defect in the application: Provided that the Adjudicating Authority shall, before rejecting the application, give a notice to the applicant to rectify the defect in his application **within seven days** of receipt of such notice from the Adjudicating Authority. It is applicable for all kind of applications filed i.e. by Financial Creditor or Operational Creditor or by the Corporate Debtor.

- (5) **Commencement of corporate insolvency resolution process:** The corporate insolvency resolution process shall commence from the date of admission of the application.

- (6) **Communication of Order:** The Adjudicating Authority shall communicate order of admission or rejection of such application within seven days, as the case may be —

- (1) in case of admission, to the financial creditor and the corporate debtor;
- (2) In case of rejection, to the financial creditor [Section 7]

- (7) **Withdrawal of application:** Withdrawal of application shall be pursuant to Section 12A of the Code read with Regulation 30A of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016. The following scenarios may arise for withdrawal of application:

1. Before admission of application

An application initiating CIRP may be withdrawn before its admission, at any time with the permission of the Adjudicating Authority. [Rule 8 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016]

2. After admission of application

Once application is admitted, further three scenarios may arise:

(a) Before Constitution of CoC

- The applicant shall make an application for withdrawal to the Adjudicating Authority through the interim resolution professional;

(b) After Constitution of CoC but before issue of Invitation for Expression of Interest ("EoI")

- An application for withdrawal shall be firstly considered by the CoC, within seven days of its receipt.
- Such withdrawal application shall be approved by the CoC with ninety percent voting share,
- upon which the resolution professional shall submit such withdrawal application along with the approval of the committee,
- to the Adjudicating Authority on behalf of the applicant,
- within three days of such approval.

(c) After issue of invitation for EoI

- The same procedure as stipulated for scenario 'b' above shall apply.
- However, in this scenario, the applicant shall state the reasons justifying withdrawal after issue of such invitation.

In all the above scenarios, the final approval of such withdrawal shall be by way of an order passed by the Adjudicating Authority.

Case Laws

1. National Company Law Tribunal, Mumbai Bench in *Bank of India v. Future Retail Ltd.* in 2022, came with an issue, where a financial creditor had provided various credit facilities and non-fund-based limits to corporate debtor. It were restructured under a sanctioned letter and framework agreement. Corporate debtor defaulted in repayment and account of corporate debtor was classified as a non-performing asset (NPA). Meanwhile, corporate debtor issued a letter to financial creditor and certain other lenders for one-time restructuring (OTR) facilities under 'resolution frame work agreement for Covid 19 related stress as per RBI Circular. Financial creditor considered corporate debtor's request allowing OTR and executed a framework agreement for restructuring of existing outstanding amount. However, corporate debtor again defaulted in repayment of an outstanding amount. Financial creditor filed petition under section 7. It was noted that corporate debtor, on payment obligation under OTR scheme, admitted default of its repayment and further, corporate debtor admitted outstanding amount in its meeting with lenders that events of default continued to subsist. It was held, in view of facts, that existence of debt and default had been proved and, therefore, petition filed by financial creditor to initiate CIRP against corporate debtor was admitted.

2. National Company Law Appellate Tribunal, New Delhi, in 2022 in *Siti Networks Ltd. v. Assets Care and Reconstruction Enterprises Ltd.* decided on continuation of proceeding by assignee on an application seeking substitution as financial creditor in place of original financial creditor.

In the given case, financial creditor sanctioned a loan to corporate debtor, however, corporate debtor failed and was classified as non-performing asset. Financial creditor filed an application under section 7 against corporate debtor and same was admitted by NCLT. Later, financial creditor vide registered assignment deed, assigned debt of corporate debtor to respondent i.e. assignee. Corporate debtor was informed about aforesaid assignment. Subsequently, assignee filed an application seeking substitution as financial creditor in place of original financial creditor and was permitted by NCLT to pursue application filed by original financial creditor. Challenging said order, instant appeal was filed by corporate debtor. It was held that section 5(7) of the Code defines financial creditor, also includes a person to whom such debt has been legally assigned or transferred to. Therefore by virtue of assignment, assignee became financial creditor and had stepped in shoes of original financial creditor and assignee had every right to continue proceeding, which was initiated by original financial creditor.

3. SC in *Manish Kumar v. Union of India* in 2021 came up with a decision on section 7 by section 3 of IBC (Amendment) Act, 2020 requiring minimum threshold for initiation of proceedings (class action) by certain categories of financial creditors against corporate debtors such as real estate developers, are Constitutionally Valid.

In the given case, CIRP was initiated by the Financial creditors requiring minimum threshold for initiation of proceedings (class action) by certain categories of financial creditors against corporate debtors such as real estate developers.

According to Provisos of section 7, it was required that in case of a real estate project, being conducted by a corporate debtor, an application can be filed by either one hundred allottees or allottees constituting one-tenth of allottees, whichever is less, if they are able to establish a default in regard to a financial creditor and it is not necessary that there must be default *qua* any of Applicants. It was held that since default can be *qua* any of applicants and even a person who is not an applicant and action is one which is understood to be in rem, in that, procedures under Code would bind entire set of stakeholders including whole of allottees.

(B) Initiation of corporate insolvency resolution process by operational creditor

- (1) Serving of demand Notice:** On the occurrence of default, an operational creditor shall first send a demand notice and a copy of invoice to the corporate debtor in such form and manner as may be ⁴prescribed.

"Demand notice" means a notice served by an operational creditor to the corporate debtor demanding payment of the operational debt in respect of which the default has occurred.

On receipt of demand notice by corporate debtor: The corporate debtor shall, within a period of ten days of the receipt of the demand notice or copy of the invoice, bring to the notice of the operational creditor about-

- (a) **existence of a dispute about debt**, if any, record of the pendency of the suit or arbitration proceedings filed before the receipt of such notice or invoice in relation to such dispute;
- (b) **the payment of unpaid operational debt**— It is possible that corporate debtor might have already paid the unpaid operational debt, there in such situation, corporate debtor will inform within 10 days -
 - (i) by sending an attested copy of the record of electronic transfer of the unpaid amount from the bank account of the corporate debtor; or
 - (ii) by sending an attested copy of record that the operational creditor has encashed a cheque issued by the corporate debtor. [Section 8]

(2) Application for initiation of Corporate Insolvency Resolution Process by operational creditor after issue of demand notice:

- (i) **Filing of application by operational creditor:** If no reply is received or payment or notice of the dispute under section 8(2) from the corporate debtor within ten days from the date of delivery of the notice or invoice demanding payment, or even if reply is received disputing the claim and operations creditors feels that the dispute is vague or untenable, operational creditor can file application⁵ before Adjudicating Authority (NCLT) for initiating a corporate insolvency resolution process.
- (ii) **Providing of documents/ information:** The operational creditor shall, along with the application filed in prescribed form, furnish the following documents—

⁴ Rule 5, Form 3 & Form 4 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016.

⁵ Rules 6, 8, 9 & 10 and Form 5 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016

a copy of the invoice , or demand notice

- demanding payment, or delivered by the operational creditor to the corporate debtor;

an affidavit

- to the effect that there is no notice given by the corporate debtor relating to a dispute of the unpaid operational debt

a copy of the certificate

- from the financial institutions maintaining accounts of the operational creditor confirming that there is no payment of an unpaid operational debt by the corporate debtor, if available;

a copy of a record with information utility

- confirming that there is no payment of an unpaid operational debt by the corporate debtor, if available; and

any other proof

- confirming that there is no payment of an unpaid operational debt by the corporate debtor, or

such other information,

- as may be prescribed.

- (3) **Appointment of IRP:** An operational creditor initiating a corporate insolvency resolution process, may propose a insolvency professional to act as an interim resolution professional.
- (4) **Order of an adjudicating authority:** The Adjudicating Authority shall, within fourteen days of the receipt of the application, by an order—

admit the application and communicate such decision to the operational creditor and the corporate debtor if,—	reject the application and communicate such decision to the operational creditor and the corporate debtor, if—
(a) the application made is complete; (b) there is no payment of the unpaid operational debt; (c) the invoice or notice for payment to the corporate debtor has been delivered by the operational creditor; (d) no notice of dispute has been received by the operational creditor or there is no record of dispute in the information utility; and (e) there is no disciplinary proceeding pending against any resolution professional proposed, if any.	(a) the application made is incomplete; (b) there has been payment of the unpaid operational debt; (c) the creditor has not delivered the invoice or notice for payment to the corporate debtor; (d) notice of dispute has been received by the operational creditor or there is a record of dispute in the information utility; or (e) any disciplinary proceeding is pending against any proposed resolution professional: Provided that Adjudicating Authority, shall before rejecting an application which is incomplete, give a notice to the applicant to rectify the defect in his application within seven days of the date of receipt of such notice from the adjudicating Authority.

- (5) **Withdrawal of application before or after admission:** The same procedure as stated under initiation of CIRP by financial creditor shall apply here as well for withdrawal of application.
- (6) **Commencement of insolvency resolution process:** The corporate insolvency resolution process shall commence from the date of admission of the application [Section 9]

Case Laws

1. SC in the matter of *Mobilox Innovations Pvt. Ltd. Vs. Kirusa Software Pvt. Ltd.* Civil Appeal No. 9405 of 2017 dt 21st Sept 2017. It was decided that in sec 9 application if there is dispute then it cannot be admitted. It should not feeble legal argument or an assertion of facts unsupported by evidence and it need not be spurious, mere bluster, plainly frivolous or vexatious.
2. National Company Law Appellate Tribunal, Chennai in *Fipola Retail (India) (P.) Ltd. v. M2N Interiors* in 2021 admitted application filed by operational creditor under section 9 against corporate debtor in name of proprietary concern. Corporate debtor alleged that said application would not be maintainable as application had been filed in name of proprietary concern which is not a 'person' for purpose of filing application under section 9. It was held that such an application was maintainable, as section 2(f) provides that provisions of Code shall apply to partnership firms and proprietorship firm also.

(C) Initiation of corporate insolvency resolution process by corporate applicant.

- (1) **Commission of default:** Where a corporate debtor has committed a default, a **corporate applicant** thereof may file an application for initiating corporate insolvency resolution process with the Adjudicating Authority. The application shall be filed in such form, containing such particulars and in such manner and accompanied with such fee as may be prescribed.⁶

"Corporate applicant means – (a) Corporate debtor, or (b) a member or partner of the corporate debtor who is authorised to make an application for the corporate insolvency resolution process under the **constitutional document** of the corporate debtor; or (c) an individual who is in charge of managing the operations and resources of the corporate debtor; or (d) a person who has the control and supervision over the financial affairs of the corporate debtor;

"constitutional document", in relation to a corporate person, includes articles of association, memorandum of association of a company and incorporation document of a Limited Liability Partnership;

- (2) **Furnishing of information:** The corporate applicant shall, along with the application furnish the information relating to—

⁶ Rules 7, 8, 9 & 10 & Form 6 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016

- (a) its **books of account and such other documents** relating to such period as may be specified; and
 - (b) the **insolvency professional** proposed to be appointed as an interim resolution professional.
 - (c) **special resolution** passed by shareholders of the corporate debtor or the resolution passed by at least three-fourth of the total number of partners of the corporate debtor, as the case may be, approving filing of the application.
- (3) **Admission/rejection of application:** The Adjudicating Authority shall, within a period of fourteen days of the receipt of the application, by an order—
- (a) admit the application, if it is complete; and no disciplinary proceeding is pending against the proposed resolution professional
 - (b) reject the application, if it is incomplete or any disciplinary proceeding is pending against the proposed resolution professional

Provided that Adjudicating Authority shall, before rejecting an application, give a notice to the applicant to rectify the defects in his application within seven days from the date of receipt of such notice from the Adjudicating Authority.

Case Law

NCLT Mumbai Bench in CP (IB) 918/MB/C-II/2020 dt. 10th Oct 2020 in the matter of *IGOPL Offshore P Ltd* has pronounced that section 10(3)(c) of the Code requires that a Special Resolution passed by the shareholders of the Corporate Debtor needs to be filed along with the Company Petition.

- (4) **Commencement of insolvency resolution process:** The corporate insolvency resolution process shall commence from the date of admission of the application. [Section 10]

(III) Suspension of initiation of corporate insolvency resolution process

Notwithstanding anything contained in sections 7, 9 and 10, no application for initiation of corporate insolvency resolution process of a corporate debtor shall be filed, for any default arising on or after 25th March, 2020 for a period of six months or such further period, not exceeding one year from such date, as may be notified in this behalf:

Provided that no application shall ever be filed for initiation of corporate insolvency resolution process of a corporate debtor for the said default occurring during the said period.

Explanation- For the removal of doubts, it is hereby clarified that the provisions of this section shall not apply to any default committed under the said sections before 25th March, 2020. [Section 10A]

The provisions of section 10A was extended twice and it was applicable for default up to 25/3/2021.

(IV) Persons not entitled to initiate insolvency process

Following persons shall not be entitled to initiate the corporate insolvency process:-

- (a) A corporate debtor undergoing an insolvency resolution process or a pre-packaged insolvency resolution process; or
- (aa) A financial creditor or an operational creditor of a corporate debtor undergoing a pre-packaged insolvency resolution process; or
- (b) A corporate debtor having completed corporate insolvency resolution process 12 (twelve) months preceding the date of making of the application; or
- (ba) a corporate debtor in respect of whom a resolution plan has been approved under Chapter III-A, twelve months preceding the date of making of the application; or
- (c) A corporate debtor or a financial creditor who has violated any of the terms of resolution plan which was approved 12 (twelve) months before the date of making of an application;
- (d) A corporate debtor in respect of whom a liquidation order has been made.

Explanation 1 - For the purposes of this section, a corporate debtor includes a corporate applicant in respect of such corporate debtor.

Explanation 2- For the purposes of this section, it is hereby clarified that nothing in this section shall prevent a corporate debtor referred to in clauses (a) to (d) from initiating corporate insolvency resolution process against another corporate debtor. [Section 11]

Following categories of Corporate debtors not entitled to file an application under section 11

- Corporate debtor undergoing CIRP/PPIRP
- A financial creditor / operational creditor undergoing a PPIRP
- Corporate debtor having completed CIRP 12 months before the date of making of the application
- a corporate debtor in respect of whom a resolution plan has been approved under Chapter III-A, 12 months preceding the date of making of the application
- Corporate debtor violating the term of resolution plan
- Corporate debtor in respect of whom a liquidation order has been made

Example: Suppose ABC LLP ("Corporate Debtor") has committed a default. Mr. X and Mr. Y, are partners of the Corporate Debtor contributing to the capital and sharing profits/losses in the ratio of 49% and 51% respectively. However, Mr. Y under the constitutional document of the Company, is being authorized to make an application for the corporate insolvency resolution process. Being a partner of the Corporate Debtor, Mr. Y filed an application on behalf of the Corporate Debtor for initiation of corporate insolvency resolution process.

As per section 10 of the Code, initiation of CIRP by a Corporate Debtor shall be made by filing an application along with information relating to books of accounts, interim resolution professional and resolution passed by at least three-fourths of total number of partners. In the given case, even though Mr. Y is authorized to file an application for initiation of CIRP, such act shall not stand valid if the resolution authorizing such filing has not been passed by at least three-fourths of total number of partners.

(V) Disposal of applications under section 54C and under section 7 or section 9 or section 10

- (1) Where an application filed under section 54C is pending, the Adjudicating Authority shall pass an order to admit or reject such application under section 54C, before considering any application filed under section 7 or section 9 or section 10, in respect of the same corporate debtor.
- (2) Where an application under section 54C is filed within fourteen days of filing of any application under section 7 or section 9 or section 10, which is pending, in respect of the same corporate debtor, then, notwithstanding anything contained in sections 7, 9 or 10, the Adjudicating Authority shall first dispose of the application under section 54C.
- (3) Where an application under section 54C is filed after fourteen days of the filing of any application under section 7 or section 9 or section 10, in respect of the same corporate debtor, the Adjudicating Authority shall first dispose of the application under sections 7, 9 or 10.
- (4) The provisions of this section shall not apply where an application under section 7 or section 9 or section 10 is filed and pending as on the date of the commencement of the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2021. [Section 11A]

(VI) Adjudication: Admission or Rejection of Application

The Adjudicating Authority may either accept or reject the application within fourteen days of receipt of application. However, applicant should be allowed to rectify the defect within seven days of receipt of notice of such rejection.

The insolvency resolution process shall commence from the date of admission of application by the Adjudicating Authority. It is referred to as the Insolvency Commencement Date.

(VII) Time-limit for completion of insolvency resolution process

- (1) **Period for completion of insolvency process:** The corporate insolvency resolution process shall be completed within a period of **one hundred and eighty days** from the date of admission of the application to initiate such process.
- (2) **Filing of application for extension of period:** The resolution professional shall file an ⁷application to the Adjudicating Authority to extend the period of the corporate insolvency resolution process beyond one hundred and eighty days, if instructed to do so by a resolution

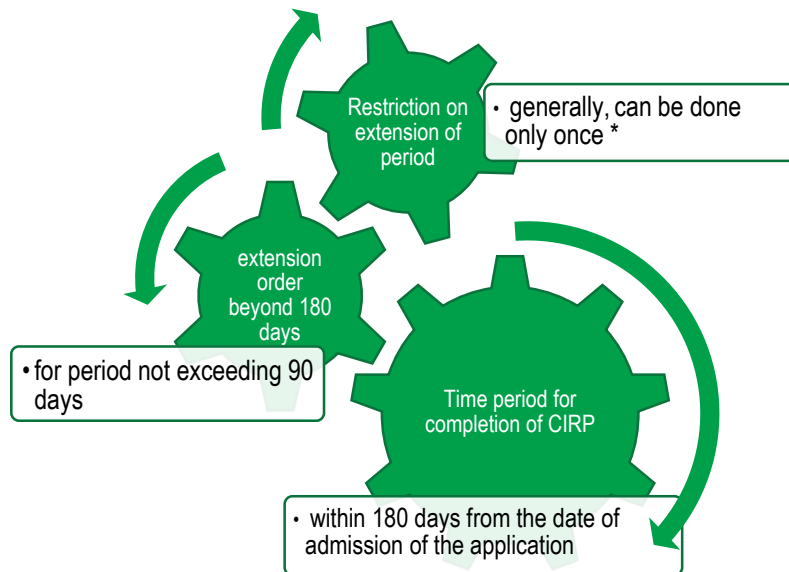
⁷ Under Regulation 40 of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016

passed at a meeting of the committee of creditors by a vote of sixty- six per cent (minimum) of the voting shares.

- (3) **Period of extension:** On receipt of an application, if the Adjudicating Authority is satisfied that the subject matter of the case is such that corporate insolvency resolution process cannot be completed within one hundred and eighty days, it may by order extend the duration of such process beyond one hundred and eighty days by such further period as it thinks fit, **but not exceeding ninety days:** Provided that any extension of the period of corporate insolvency resolution process under this section shall not be granted more than once.

Provided further that the corporate insolvency resolution process shall mandatorily be completed within a period of **three hundred and thirty days** from the insolvency commencement date, including any extension of the period of corporate insolvency resolution process granted under this section and the time taken in legal proceedings in relation to such resolution process of the corporate debtor:

Provided also that where the insolvency resolution process of a corporate debtor is pending and has not been completed within the period referred to in the second proviso, such resolution process shall be completed within a period of ninety days from the date of commencement of the Insolvency and Bankruptcy Code (Amendment) Act, 2019.



* Adjudicating Authority (NCLT) has power to extend the CIRP period beyond 270 days on the basis of reasonable justifications, in the interest of furtherance of the objectives of the Code.

(VIII) Appointment of Interim Resolution Professional

"Resolution Professional", means an insolvency professional appointed to conduct the corporate insolvency resolution process and includes an interim resolution professional.

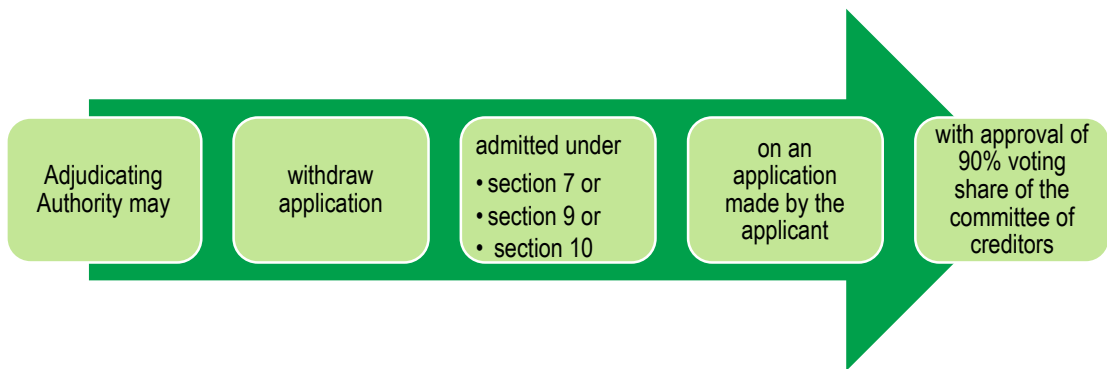
If applicant proposes for appointment of Insolvency professional

- obtain written communication from insolvency professional for appointment as interim resolution professional

(IX) Withdrawal of application admitted under section 7, 9 or 10 [Section 12A]

(1) **Before formation of Committee of Creditors:** Application can be withdrawn if settlement is there with the creditor and appropriate form is filed through IRP.

(2) **After Committee of Creditors is formed:**

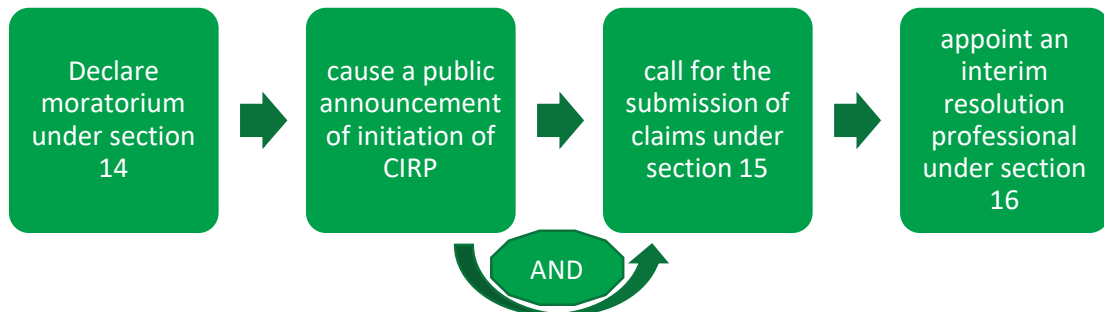


Case Law

SC in *Ashok G. Rajani v. Beacon Trusteeship Ltd.* said that Section 12A enables the NCLT to allow the withdrawal of an application admitted under section 7 or section 9 or section 10, on an application made by the applicant with the approval of 90 per cent voting shares of the Committee of Creditors. Section 12A clearly permits withdrawal of an application under section 7 that has been admitted on an application made by the applicant. The question of approval of the Committee of Creditors by the requisite percentage of votes, can only arise after the Committee of Creditors is constituted. Before the Committee of Creditors is constituted, there is, no bar to withdrawal by the applicant of an application admitted under section 7.

(X) Declaration of moratorium and public announcement:

After admission of application, the Adjudicating Authority shall pass following order —



The public announcement as referred above, shall be made immediately after the appointment of the interim resolution professional. **[Section 13]**

Moratorium:

Moratorium is a delay or suspension of an activity. In a legal context, it may refer to the temporary suspension of a law to allow a legal challenge to be carried out.

After the commencement of corporate insolvency resolution process a calm period, known as moratorium period is declared, during which all suits and legal proceedings etc. against the Corporate Debtor are held in abeyance to allow the IRP/ RP to carry out his/her task smoothly and disallowing creditors and other stakeholders to take any individual actions against the corporate debtor and disrupt the process.

- (1) **Declaration of moratorium period:** According to the section 14(1) of the Code, on the insolvency commencement date, the Adjudicating Authority shall by order, declare moratorium prohibiting all of the following, acts—
 - (a) **the institution of suits or continuation of pending suits or proceedings** against the corporate debtor including execution of any judgment, decree or order in any court of law, tribunal, arbitration panel or other authority;
 - (b) **transferring, encumbering, alienating or disposing of** by the corporate debtor any of its assets or any legal right or beneficial interest therein;
 - (c) **any action to foreclose, recover or enforce any security interest** created by the corporate debtor in respect of its property including any action under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;
 - (d) **the recovery of any property** by an owner or lessor where such property is occupied by or in the possession of the corporate debtor.

Explanation—For the purposes of this sub-section, it is hereby clarified that notwithstanding anything contained in any other law for the time being in force, a licence, permit, registration, quota, concession, clearance or a similar grant or right given by the Central Government, State Government, local authority, sectoral regulator or any other authority constituted under any other law for the time being in force, shall not be suspended or terminated on the grounds of insolvency, subject to the condition that there is no default in payment of current dues arising for the use or continuation of the license or a similar grant or right during moratorium period

- (2) **The supply of essential goods or services⁸** to the corporate debtor as may be specified shall not be terminated or suspended or interrupted during moratorium period.

⁸ Regulation 32 of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016

- (2A) Where the interim resolution professional or resolution professional, as the case may be, considers the supply of goods or services critical to protect and preserve the value of the corporate debtor and manage the operations of such corporate debtor as a going concern, then the supply of such goods or services shall not be terminated, suspended or interrupted during the period of moratorium, except where such corporate debtor has not paid dues arising from such supply during the moratorium period or in such circumstances as may be specified
- (3) **Prohibited Acts:** Acts prohibited during Moratorium period, shall not apply to-
- (a) Such transactions as may be notified by the Central Government in consultation with any financial sector regulator.
 - (b) A surety in a contract of guarantee to a corporate debtor.
- (4) **Effect of the order of moratorium:** The order of moratorium shall have effect from the date of such order till the completion of the corporate insolvency resolution process:

The provision of section 14(1) of the Code is not applicable on a surety in a contract of guarantee to a corporate debtor. Thus, recovery proceedings, insolvency resolution process or bankruptcy proceedings against surety (guarantor) can be initiated even if moratorium is granted to corporate debtor.

It is clarified that notwithstanding anything contained in any other law for the time being in force, a licence, permit, registration, quota, concession, clearance or a similar grant or right given by the Central Government, State Government, local authority, sectoral regulator or any other authority constituted under any other law for the time being in force, shall not be suspended or terminated on the grounds of insolvency, subject to the condition that there is no default in payment of current dues arising for the use or continuation of the license or a similar grant or right during moratorium period.

When Moratorium period shall cease to have effect

Provided that where at any time during the corporate insolvency resolution process period, if the Adjudicating Authority approves the resolution plan or passes an order for liquidation of corporate debtor, the moratorium shall cease to have effect from the date of such approval or liquidation order, as the case may be [Section 14]

Example: After commencement of Corporate Insolvency Resolution Process, NCLT declared Moratorium against the corporate debtor. Within a month of declaration, corporate debtor disposed of his property. In line with section 14 of the Code, any transaction/disposal of any assets of Corporate Debtor during the moratorium period, is prohibited. Such an act of the Corporate Debtor is not valid.

However, as per Regulation 29 of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016, the Resolution Professional may sell unencumbered asset(s) of the corporate debtor, other than in the ordinary course of business, not exceeding 10% of the total claims admitted.

Public Announcement

Interim Resolution Professional shall make the Public Announcement immediately after his appointment. "Immediately" refers to not more than **three days** from the date of appointment of the Interim Resolution Professional.

Particulars of the Public announcement: As per **Section 15** of the Code, public announcement shall include the followings and it shall be in the form prescribed :-

- a) Name & Address of Corporate Debtor under the Corporate Insolvency Resolution Process.
- b) Name of the authority with which the corporate debtor is incorporated or registered.
- c) Details of interim resolution Professional who shall be vested with the management of the Corporate Debtor and be responsible for receiving claims.
- d) Penalties for false or misleading Claims.
- e) The last date for the submission of the claims as may be specified.
- f) The date on which the Corporate Insolvency Resolution Process ends.

The expenses of public announcement shall be borne by the applicant or which may be reimbursed by the Committee of Creditors, to the extent it ratifies them.

(XI) Appointment, Term and Powers of Interim Resolution Professional (IRP)

Appointment of IRP: Adjudicating authority shall appoint an Interim Resolution Professional on the insolvency commencement date. Section 16 of the Code lays down the procedure for appointment of an Interim Resolution Professional.

Where the application for corporate insolvency resolution process is made by a financial creditor or the corporate debtor, the resolution professional as proposed in the application shall be appointed as the interim resolution professional, if no disciplinary proceedings are pending against him.

Where the **application for corporate insolvency resolution process is made by an operational creditor** and

- (a) **No name of an interim resolution professional is made.** The Adjudicating Authority shall make a reference to the Board for the recommendation of an insolvency professional who may be appointed to act as an interim resolution professional.
- (b) **A name of an interim resolution professional is made** the proposed resolution professional shall be appointed as the interim resolution professional, if no disciplinary proceedings are pending against him.

The Board shall recommend the name of an insolvency professional to the Adjudicating Authority against whom no disciplinary proceedings are pending, within ten days of the receipt of a reference from the Adjudicating Authority.

Period of appointment of IRP: The term of Interim Resolution Professional shall continue till the date of appointment of the resolution professional under section 22. **[Section 16]**

The key duties to be performed by the Interim Resolution Professional are:-

- (a) collect all information relating to the **assets, finances and operations of the corporate debtor** for determining the financial position of the corporate debtor
- (b) **Collation of claims** received pursuant to public announcement made
- (c) **Constitution of the Committee of Creditors**
- (d) **monitor the assets** of the corporate debtor **and manage its operations** until a resolution professional is appointed by the committee of creditors
- (e) **File information** collected with the information utility, if necessary
- (f) Take **control and custody of any assets** over which corporate debtor has ownership rights
- (g) **Perform other duties** as specified by the Board **[Section 18]**

Powers of IRP: As per section 17 of the Code, from the date of appointment of the interim resolution professional, the management of the affairs of the corporate debtor shall vest in the IRP—

- (a) The management of the affairs of the corporate debtor shall vest in the interim resolution professional. IRP shall be authorized to do the following:
 - act and execute in the name and on behalf of the corporate debtor all deeds, receipts, and other documents, if any;
 - take such actions, in the manner and subject to such restrictions, as may be specified by the Board;
 - have the authority to access the electronic records of corporate debtor from information utility having financial information of the corporate debtor;
 - have the authority to access the books of account, records and other relevant documents of corporate debtor available with government authorities, statutory auditors, accountants and such other persons as may be specified; and
 - be responsible for complying with the requirements under any law for the time being in force on behalf of the corporate debtor.
- (b) **Exercise of Power of BoD/ partners:** The powers of the board of directors or the partners of the corporate debtor, as the case may be, shall stand suspended and be exercised by the interim resolution professional.
- (c) **Reporting of officers/managers:** The officers and managers of the corporate debtor shall report to the interim resolution professional and provide access to such documents and records of the corporate debtor as may be required by the interim resolution professional.

- (d) **Instructions to financial institutions:** The financial institutions maintaining accounts of the corporate debtor shall act on the instructions of the interim resolution professional in relation to such accounts and furnish all information relating to the corporate debtor available with them to the interim resolution professional.

Management of operations of corporate debtor as going concern: The IRP shall make every endeavor to protect and preserve the value of the property of the corporate debtor and manage the operations of the corporate debtor as a going concern.

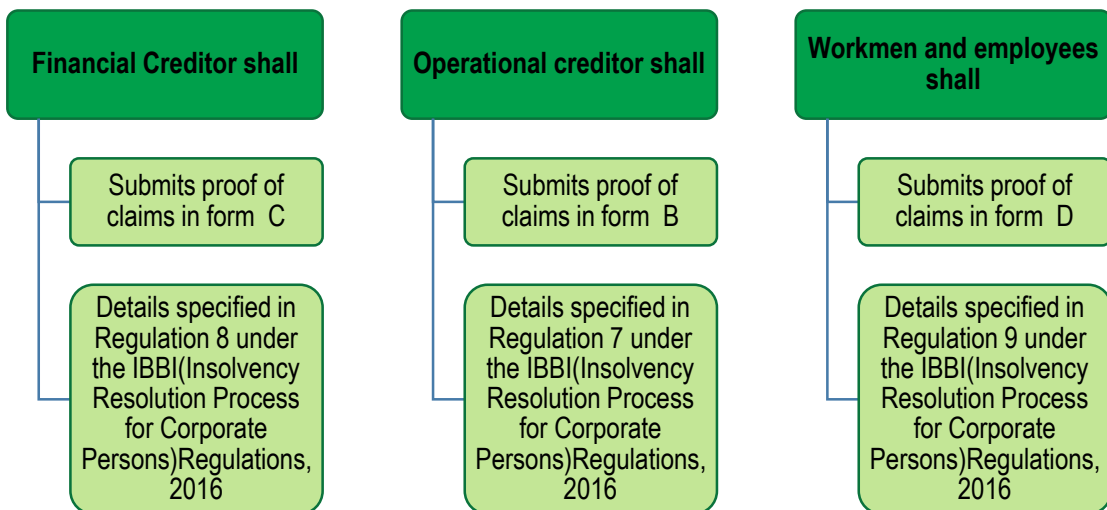
The interim resolution professional shall have the authority—

- (a) to appoint accountants, legal or other professionals as may be necessary;
- (b) to enter into contracts on behalf of the corporate debtor or to amend or modify the contracts or transactions which were entered into before the commencement of corporate insolvency resolution process;
- (c) to raise interim finance provided that no security interest shall be created over any encumbered property of the corporate debtor without the prior consent of the creditors whose debt is secured over such encumbered property:

Provided that no prior consent of the creditor shall be required where the value of such property is not less than the amount equivalent to twice the amount of the debt.

- (d) to issue instructions to personnel of the corporate debtor as may be necessary for keeping the corporate debtor as a going concern; and
 - (e) to take all such actions as are necessary to keep the corporate debtor as a going concern.
- [Section 20]**

Manner of submission of proof of claims to IRP: Proofs of claim shall be committed to IRP as follows:



A creditor shall submit claim with proof on or before the last date mentioned in the public announcement. The IRP shall verify such claims within 7 days from the last date of receipt of the claims and within two days of such verification of claims, file a report to the Adjudicating Authority, certifying constitution of the CoC.

However, a creditor, who fails to submit claim with proof within the time stipulated in the public announcement, may submit the claim with proof to the interim resolution professional or the resolution professional, as the case may be, on or before the ninetieth day of the insolvency commencement date. The IRP or the RP, as the case may be, shall verify every claim and thereupon maintain a list of creditors. Such list of creditors shall be filed with the Adjudicating Authority and also, displayed on the website, if any, of the Corporate Debtor.

(XII) Resolution Professional (RP)

Appointment: As per **Section 22** of the Code, the first meeting of the committee of creditors shall be held within seven days of the constitution of the committee of creditors.

The Committee of Creditors in the first meeting by majority vote of not less than 66% of the Voting Share of the Financial Creditors either-

- **resolve to appoint** the interim resolution professional as a Resolution Professional, or
- **to replace** the interim resolution professional by another Resolution Professional.

Where the committee of creditors resolves—

- (a) **to continue the interim resolution professional as resolution professional** subject to a written consent from the interim resolution professional in the specified form, it shall communicate its decision to the interim resolution professional, the corporate debtor and the Adjudicating Authority; or
- (b) **to replace the interim resolution professional**, it shall file an application before the Adjudicating Authority for the appointment of the proposed resolution professional along with a written consent from the proposed resolution professional in the specified form.

The Adjudicating Authority shall forward the name of the resolution professional proposed to the Board for its confirmation and shall make such appointment after confirmation by the Board.

Where the Board does not confirm the name of the proposed resolution professional within ten days of the receipt of the name of the proposed resolution professional, the Adjudicating Authority shall, by order, direct the interim resolution professional to continue to function as the resolution professional until such time as the Board confirms the appointment of the proposed resolution professional.

Example: Mr. Z was the Interim Resolution Professional (IRP) in XY Company. The committee of creditors by majority vote of financial creditors proposed to appoint Mr. Final as Resolution professional (RP) of the XY Company. The said proposal was confirmed by the Board after 10

days. As per Section 22 of the Code, if Board does not confirm the proposed name as RP within 10 days of receipt of proposal, the Adjudicating authority shall direct IRP i.e., Mr. Z to continue as RP for such time as the Board confirms for the appointment of proposed RP.

Role and Duties of RP: The primary role and duty of RP is to conduct corporate insolvency resolution process and to preserve and protect the assets of the corporate debtor, including the continued business operations of the corporate debtor.

- (1) RP shall conduct the entire corporate insolvency resolution process and manage the operations of the corporate debtor during the corporate insolvency resolution process period.

Provided that the resolution professional shall continue to manage the operations of the corporate debtor after the expiry of the corporate insolvency resolution process period, until an order approving the resolution plan under sub-section (1) of section 31 or appointing a liquidator under section 34 is passed by the Adjudicating Authority.

- (2) RP shall exercise powers and perform duties as are vested or conferred on the interim resolution professional under this Chapter.
- (3) In case of any appointment of a resolution professional other than IRP, the interim resolution professional shall provide all the information, documents and records pertaining to the corporate debtor in his possession and knowledge to the resolution professional. **[Section 23]**

Duties: It shall be the duty of the resolution professional to preserve and protect the assets of the corporate debtor, including the continued business operations of the corporate debtor. The resolution professional shall undertake the following actions to protect the assets of the corporate debtor, namely:—

- (a) take immediate custody and control of all the assets of the corporate debtor, including the business records of the corporate debtor;
- (b) represent and act on behalf of the corporate debtor with third parties, exercise rights for the benefit of the corporate debtor in judicial, quasi-judicial or arbitration proceedings;
- (c) raise interim finances subject to the approval of the committee of creditors;
- (d) appoint accountants, legal or other professionals in the manner as specified by Board;
- (e) maintain an updated list of claims;
- (f) convene and attend all meetings of the committee of creditors;
- (g) prepare the information memorandum;
- (h) invite prospective resolution applicants, who fulfil such criteria as may be laid down by him with the approval of committee of creditors, having regard to the complexity and scale of

operations of the business of the corporate debtor and such other conditions as may be specified by the Board, to submit a resolution plan or plans;

- (i) present all resolution plans at the meetings of the committee of creditors;
- (j) file application for avoidance of transactions in accordance with Chapter III, if any; and
- (k) such other actions as may be specified by the Board. **[Section 25]**

Eligibility of an insolvency Professional to be appointed as a Resolution Professional: As per Regulation 3 of Insolvency and Bankruptcy (Insolvency Resolution process for corporate persons) Regulation, 2016, an insolvency professional shall be eligible for appointment as an interim resolution or a resolution professional for a corporate insolvency process if he and all partners and directors of the insolvency professional entity of which he is partner or director are independent of the corporate debtor:-

- (a) He is eligible to be appointed as an independent director on the board of the corporate debtor under section 149 of the Companies Act, 2013, where the corporate debtor is a company.
- (b) He is not a related party of the corporate debtor.
- (c) He is not an employee or proprietor or a partner of a firm of auditors or secretarial auditors in practice or cost auditors of the corporate debtor in the last three financial years.
- (d) He is not an employee or proprietor or a partner of a legal or consulting firm that has or had any transaction with the corporate debtor amounting to five per cent or more of the gross turnover of such firm in the last three financial years.

Fees of Resolution Professional: As per Section 5(13) of the Code, the fees payable to any person acting as a resolution professional and any costs incurred by the resolution professional in running the business of the corporate debtor as a going concern shall be included in the insolvency resolution process costs and shall be paid in priority before payment to any other creditor. Recently IBBI has come out with the Circular, mandating minimum fees to be paid to the Resolution Professional. (Schedule II of IBBI (IRPCP) Regulations)

Replacement of Resolution Professional: As per the Section 27 of the Code, RP shall be replaced in the following manner:

- If at any time during the Corporate Insolvency Resolution Process the Committee of creditors is of the opinion that the resolution professional appointed is required to be replaced, they may apply to the Adjudicating Authority for replacement of such professional.
- As per Section 27 of the Code, the committee of creditors may, at a meeting, by a vote of sixty-six per cent of voting shares, resolve to replace the resolution professional appointed under section 22 with another resolution professional, subject to a written consent from the proposed resolution professional in the specified form.
- The Committee of Creditors shall forward the name of the new proposed Insolvency

Professional to the Adjudicating Authority, and Adjudicating Authority shall forward such name to the Board for confirmation.

- After the confirmation of the proposed insolvency resolution professional by the Board he shall be appointed in the same manner as laid down in Section 16 which deals with the Appointment of IRP.
- Where any disciplinary proceedings are pending against the proposed resolution professional, the resolution professional appointed under section 22 shall continue till the appointment of another resolution professional.

Preparation of information memorandum: (1) The resolution professional shall prepare an information memorandum containing such relevant information as may be specified by the Board for formulating a resolution plan.

(2) The resolution professional shall provide to the resolution applicant access to all relevant information in physical and electronic form, provided such resolution applicant undertakes—

- (a) to comply with provisions of law for the time being in force relating to confidentiality and insider trading;
- (b) to protect any intellectual property of the corporate debtor it may have access to; and
- (c) not to share relevant information with third parties unless clauses (a) and (b) above are complied with.

"Relevant information" means the information required by the resolution applicant to make the resolution plan for the corporate debtor, which shall include the financial position of the corporate debtor, all information related to disputes by or against the corporate debtor and any other matter pertaining to the corporate debtor as may be specified. **[Section 29]**

(XIII) Committee of Creditors

Constitution of CoC: As per section 21, the **interim resolution professional** shall after collation of all claims received against the corporate debtor and determination of the financial position of the corporate debtor, **constitute a committee of creditors** (CoC).

The committee of creditors shall comprise of all the financial creditors of the corporate debtor.

When FC/ authorized representative is not entitled to participate in the CoC: for the Financial Creditor or the authorised representative of the financial creditor referred to in section 24(6), 24(6A), or 24(5), if it is a related party of the corporate debtor, shall not have any right of representation, participation or voting in a meeting of the committee of creditors:

Provided further that the first proviso shall not apply to a financial creditor, regulated by a financial sector regulator, if it is a related party of the corporate debtor solely on account of conversion or

substitution of debt into equity shares or instruments convertible into equity shares, or completion of such transactions as may be prescribed prior to the insolvency commencement date.

In case where debts owed to two or more FC: The corporate debtor owes financial debts to two or more financial creditors as part of a consortium or agreement, each such financial creditor shall be part of the committee of creditors and their voting share shall be determined on the basis of the financial debts owed to them.

In case, **any person is a financial creditor as well as an operational creditor**,—

- (a) such person **shall be a financial creditor to the extent of the financial debt owed by the corporate debtor**, and shall be included in the committee of creditors, with voting share proportionate to the extent of financial debts owed to such creditor;
- (b) such person **shall be considered to be an operational creditor to the extent of the operational debt owed by the corporate debtor** to such creditor.

Where an operational creditor has assigned or legally transferred any operational debt to a financial creditor, the assignee or transferee shall be considered as an operational creditor to the extent of such assignment or legal transfer.

In case of consortium arrangement of FC: Where the terms of the financial debt extended as part of a consortium arrangement or syndicated facility provide for a single trustee or agent to act for all financial creditors, each financial creditor may—

- (a) Authorise the trustee or agent to act on his behalf in the committee of creditors to the extent of his voting share;
- (b) Represent himself in the committee of creditors to the extent of his voting share;
- (c) Appoint an insolvency professional (other than the resolution professional) at his own cost to represent himself in the committee of creditors to the extent of his voting share; or
- (d) Exercise his right to vote to the extent of his voting share with one or more financial creditors jointly or severally.

Voting by authorised representative of class of FC: As per section 21(6A), if a financial debt is owned by a class of creditors, an insolvency professional can be appointed by adjudicating authority on receipt of application from interim Resolution professional.

Who can act as an authorised representative?

Where a financial debt is in the form of securities or deposits and the terms of the financial debt provide for appointment of a trustee or agent to act as authorised representative for all the financial creditors—

- such trustee or agent shall act on behalf of such financial creditors;

Where a financial debt is owed to a class of creditors other than the creditors covered above, the IRP shall make an application to the AA along with the list of all financial creditors, with the name of an insolvency professional

- to act as their authorised representative appointed by the Adjudicating Authority prior to the first meeting of the committee of creditors;

Where a financial debt is represented by a guardian, executor or administrator,

- such person shall act as authorised representative on behalf of such financial creditors

Authorised Representative from the State or Union Territory having highest number of creditors in class

The Interim Resolution Professional shall offer the names of three insolvency professionals to be voted upon by the class of creditors, who must be from the State or Union Territory, which has the highest number of creditors in the class as per records of the corporate debtor.

Where such State or Union Territory does not have adequate number of insolvency professionals, the insolvency professionals having addresses in a nearby State or Union Territory, as the case may be, shall be considered.

Rights of Authorised representative: Above Authorised representative shall attend the meetings of the committee of creditors, and vote on behalf of each financial creditor to the extent of his voting share.

All decisions of the committee of creditors shall be taken by a vote of not less than fifty-one per cent of voting share of the financial creditors.

Provided that where a corporate debtor does not have any financial creditors, the committee of creditors shall be constituted and shall comprise of such persons to exercise such functions in such manner as may be specified.

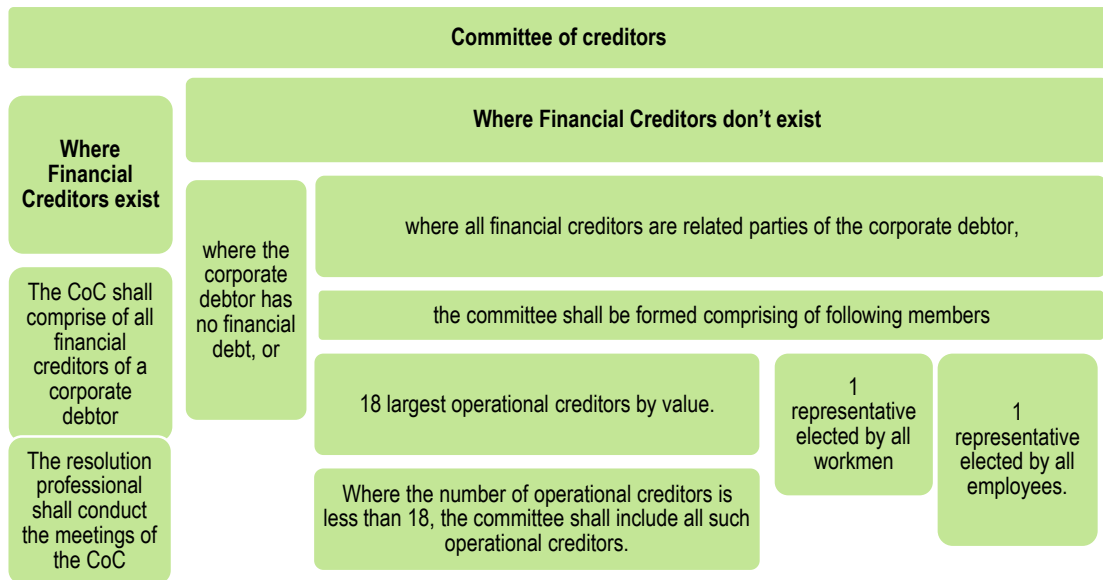
The committee of creditors shall have the right to require the resolution professional to furnish any financial information in relation to the corporate debtor at any time during the corporate insolvency resolution process.

The resolution professional shall make available any financial information so required by the committee of creditors as mentioned above within a period of seven days of such requisition.

(XIII) Meeting of committee of creditors

The provisions related to the meeting of committee of creditors are being dealt under the section 24 of the Code.

Composition: The composition of the committee shall be as follows:-



Procedure for conduct of meeting of CoC: The members of the committee of creditors may meet in person or by such electronic means. All the meeting of CoC shall be conducted by the RP. Notice of meeting shall be served to the following:

- (a) members of Committee of creditors, including the authorised representatives;
- (b) members of the suspended Board of Directors or the partners of the corporate persons, as the case may be;
- (c) operational creditors or their representatives if the amount of their aggregate dues is not less than ten per cent of the debt.

The directors, partners and one representative of operational creditors, as referred above, may attend the meetings of committee of creditors, but shall not have any right to vote in such meetings. The absence of any them shall not invalidate proceedings of such meeting. The resolution professional shall determine the voting share to be assigned to each creditor in the manner specified by the Board.

As per section 5(28) “**voting share**” means the share of the voting rights of a single financial creditor in the committee of creditors which is based on the proportion of the financial debt owed

to such financial creditor in relation to the financial debt owed by the corporate debtor. Each creditor shall vote in accordance with the voting share assigned to him based on the financial debts owed to such creditor. However voting rights of committee with only operational creditor will be in proportion to debt due to each creditor to "total debt". Whereas total debt will be equal to debts due to creditors, workmen and employees. [Regulation 16(3) of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016].

Filing of report certifying constitution of the committee

The interim resolution professional shall file a report certifying constitution of the committee to the Adjudicating Authority within two days of the verification of claims received.

First Meeting of Creditors: The interim resolution professional shall hold the first meeting of the committee within seven days of filing the report as mentioned above.

Where the appointment of resolution professional is delayed, the interim resolution professional shall perform the functions of the resolution professional from the fortieth day of the insolvency commencement date till a resolution professional is appointed under section 22 as per regulation 17 of IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016.

Meetings of the committee

- (1) A resolution professional may convene a meeting of the committee as and when he considers necessary.
- (2) On a request received from members of the committee, shall convene a meeting if the same is made by members of the committee representing thirty three per cent of the voting rights.

Explanation—For the purposes of sub-regulation (2) it is clarified that meeting (s) may be convened under this sub-regulation till the resolution plan is approved under sub-section (1) of section 31 or order for liquidation is passed under section 33 and decide on matters which do not affect the resolution plan submitted before the Adjudicating Authority.

- (3) A resolution professional may place a proposal received from members of the committee in a meeting, if he considers it necessary and shall place the proposal if the same is made by members of the committee representing at least thirty three per cent of the voting rights.

[Regulation 18 of the of IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016]

Notice for meetings of the committee

- (1) A meeting of the committee shall be called by giving not less than five days' notice in writing to every participant,
- (2) The committee may reduce the notice period from five days to such other period of not less than twenty-four hours, as it deems fit:

Provided that the committee may reduce the period to such other period of not less than forty-eight hours if there is any authorised representative. [Regulation 19 of the of IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016.]

Quorum for the Meeting

- A meeting of committee of creditors shall quorate if members of the **committee of creditors representing at least thirty-three percent of the voting rights are present** either in person or by video/audio means. Provided that the committee may modify the percentage of voting rights required for quorum in respect of any future meetings of the committee. [Regulation 22 of the of IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016]
- If the **requisite quorum for committee of creditors is not fulfilled** the meeting cannot be held and the meeting shall automatically stand adjourned at the same time and place on the next day.
- The adjourned meeting shall quorate with the members of the committee attending the meeting.

Approval of committee of creditors for certain actions:

- (1) According to section 28 of the Code, the resolution professional, during the corporate insolvency resolution process, shall not take any of the following actions without the prior approval of the committee of creditors namely:—
 - (a) **raise any interim finance** in excess of the amount as may be decided by the committee of creditors in their meeting;
 - (b) **create any security interest** over the assets of the corporate debtor;
 - (c) **change the capital structure** of the corporate debtor, including by way of issuance of additional securities, creating a new class of securities or buying back or redemption of issued securities in case the corporate debtor is a company;
 - (d) **record any change** in the ownership interest of the corporate debtor;
 - (e) **give instructions** to financial institutions maintaining accounts of the corporate debtor for a debit transaction from any such accounts in excess of the amount as may be decided by the committee of creditors in their meeting;
 - (f) **undertake any related party transaction**;
 - (g) **amend any constitutional documents** of the corporate debtor;
 - (h) **delegate its authority** to any other person;
 - (i) **dispose of or permit the disposal of shares** of any shareholder of the corporate debtor or their nominees to third parties;
 - (j) **make any change in the management** of the corporate debtor or its subsidiary;

- (k) **transfer rights or financial debts or operational debts** under material contracts otherwise than in the ordinary course of business;
 - (l) **make changes in the appointment or terms of contract** of such **personnel** as specified by the committee of creditors; or
 - (m) **make changes in the appointment or terms of contract** of **statutory auditors** or internal auditors of the corporate debtor.
- (2) The resolution professional shall convene a meeting of the committee of creditors and seek the vote of the creditors prior to taking any of the above actions.
 - (3) No action shall be approved by the committee of creditors unless approved by a vote of sixty-six per cent of the voting shares.
 - (4) Where any action is taken by the resolution professional without seeking the approval of the committee of creditors in the manner as required in this section, such action shall be void.
 - (5) The committee of creditors may report the actions of the resolution professional to the Board for taking necessary actions against him under this Code.

Voting by the committee

The resolution professional shall take a vote of the members of the committee present in the meeting, on any item listed for voting after discussion on the same.

At the conclusion of a vote at the meeting, the resolution professional shall announce the decision taken on items along with the names of the members of the committee who voted for or against the decision, or abstained from voting. [Regulation 25 of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016.]

The resolution professional shall provide each member of the committee the means to exercise its vote by either electronic means or through electronic voting system in accordance with the provisions of this Regulation

Rights and duties of authorised representative of financial creditors.

Right to vote and participate to the authorize representative in CoC Meetings: According to Section 25A of the Code, the authorised representative under section 21(6) or 21(6A) or section 24(5) shall have the right to participate and vote in meetings of the committee of creditors on behalf of the financial creditor he represents in accordance with the prior voting instructions of such creditors obtained through physical or electronic means.

To circulate the agenda and minutes: It shall be the duty of the authorised representative to circulate the agenda and minutes of the meeting of the committee of creditors to the financial creditor he represents.

To act in the interest of Financial Creditor: The authorised representative shall not act against the interest of the financial creditor he represents and shall always act in accordance with their prior instructions.

Cast of vote by authorized representative: Provided that if the authorised representative represents several financial creditors, then he shall cast his vote in respect of each financial creditor in accordance with instructions received from each financial creditor, to the extent of his voting share:

Provided further that if any financial creditor does not give prior instructions through physical or electronic means, the authorised representative shall **abstain from voting** on behalf of such creditor.

The authorised representative under section 21(6) shall cast his vote on behalf of all the financial creditors he represents in accordance with the decision taken by a vote of more than fifty per cent, of the voting share of the financial creditors he represents, who have cast their vote.

Provided that for a vote to be cast in respect of an application under section 12 A, the authorised representative shall cast his vote in accordance with the provisions of sub-section (3).

Instruction/ information filed by the authorised representative received by the FC he represents with CoC for voting: The authorised representative shall file with the committee of creditors any instructions received by way of physical or electronic means, from the financial creditor he represents, for voting in accordance therewith, to ensure that the appropriate voting instructions of the financial creditor he represents is correctly recorded by the interim resolution professional or resolution professional, as the case may be.

Explanation.—For the purposes of this section, the "electronic means" shall be such as may be specified.

Voting by Authorised Representative.

The authorised representative shall cast his vote in respect of each financial creditor or on behalf of all financial creditors he represents in accordance with the provisions of sub-section (3) or sub-section (3A) of section 25A, as the case may be. [Regulation 25A of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016.]

(XIV) Persons not eligible to be resolution applicant

One of the key duties of a Resolution professional as per section 25 of the Code is to invite prospective resolution applicants to submit resolution plans for the Corporate Debtor and present all the resolution plans before the Committee of Creditors.

Grounds of ineligibility to be a resolution applicant: Section 29A states that a person shall not be eligible to submit a resolution plan, if such person, or any other person acting jointly or in concert with such person is a/an —

- (a) is an **undischarged insolvent**;
- (b) is a **wilful defaulter** in accordance with the guidelines of the Reserve Bank of India issued under the Banking Regulation Act, 1949;
- (c) at the time of submission of the resolution plan **has an account, or an account of a corporate debtor under the management or control of such person or of whom such person is a promoter**, classified as non-performing asset in accordance with the guidelines of the Reserve Bank of India issued under the Banking Regulation Act, 1949 or the guidelines of a financial sector regulator issued under any other law for the time being in force, and at least a period of one year has lapsed from the date of such classification till the date of commencement of the corporate insolvency resolution process of the corporate debtor:

Exception : Provided that the person shall be eligible to submit a resolution plan if such person makes payment of all overdue amounts with interest thereon and charges relating to non-performing asset accounts before submission of resolution plan:

Provided further that nothing in this clause shall apply to a resolution applicant where such applicant is a financial entity and is not a related party to the corporate debtor.

Explanation I.—For the purposes of this proviso, the expression "**related party**" shall not include a financial entity, regulated by a financial sector regulator, if it is a financial creditor of the corporate debtor and is a related party of the corporate debtor solely on account of conversion or substitution of debt into equity shares or instruments convertible into equity shares, or completion of such transactions as may be prescribed prior to the insolvency commencement date.

Explanation II.—For the purposes of this clause, where a resolution applicant has an account, or an account of a corporate debtor under the management or control of such person or of whom such person is a promoter, classified as non-performing asset and such account was acquired pursuant to a prior resolution plan approved under this Code, then, the provisions of this clause **shall not apply to such resolution applicant for a period of three years** from the date of approval of such resolution plan by the Adjudicating Authority under this Code;

- (d) has been **convicted for any offence** punishable with imprisonment—
 - (i) for two years or more under any Act specified under the Twelfth Schedule; or
 - (ii) for seven years or more under any other law for the time being in force:

Provided that this clause shall not apply to a person after the expiry of a period of two years from the date of his release from imprisonment:

Provided further that this clause shall not apply in relation to a connected person referred to in clause (iii) of Explanation I;]

- (e) is **disqualified to act as a director** under the Companies Act, 2013 (18 of 2013):
Provided that this clause shall not apply in relation to a connected person referred to in clause (iii) of Explanation I;
- (f) is **prohibited by the Securities and Exchange Board of India** from trading in securities or accessing the securities markets;
- (g) has been a promoter or in the management or control of a corporate debtor in which a preferential transaction, undervalued transaction, extortionate credit transaction or fraudulent transaction has taken place and in respect of which an order has been made by the Adjudicating Authority under this Code:
Provided that this clause shall not apply if a preferential transaction, undervalued transaction, extortionate credit transaction or fraudulent transaction has taken place prior to the acquisition of the corporate debtor by the resolution applicant pursuant to a resolution plan approved under this Code or pursuant to a scheme or plan approved by a financial sector regulator or a court, and such resolution applicant has not otherwise contributed to the preferential transaction, undervalued transaction, extortionate credit transaction or fraudulent transaction;
- (h) has **executed a guarantee in favour of a creditor in respect of a corporate debtor** against which an application for insolvency resolution made by such creditor has been admitted under this Code and such guarantee has been invoked by the creditor and remains unpaid in full or part ;
- (i) is subject to **any disability**, corresponding to clauses (a) to (h), under any law in a jurisdiction outside India; or
- (j) has a **connected person** not eligible under clauses (a) to (i).

Explanation I—For the purposes of this clause, the expression "connected person" means—

- (i) any person who is the promoter or in the management or control of the resolution applicant; or
- (ii) any person who shall be the promoter or in management or control of the business of the corporate debtor during the implementation of the resolution plan; or
- (iii) the holding company, subsidiary company, associate company or related party of a person referred to in clauses (i) and (ii):

Provided that nothing in clause (iii) of Explanation I shall apply to a resolution applicant where such applicant is a financial entity and is not a related party of the corporate debtor:

Provided further that the expression "**related party**" shall not include a financial entity, regulated by a financial sector regulator, if it is a financial creditor of the corporate debtor and is a related

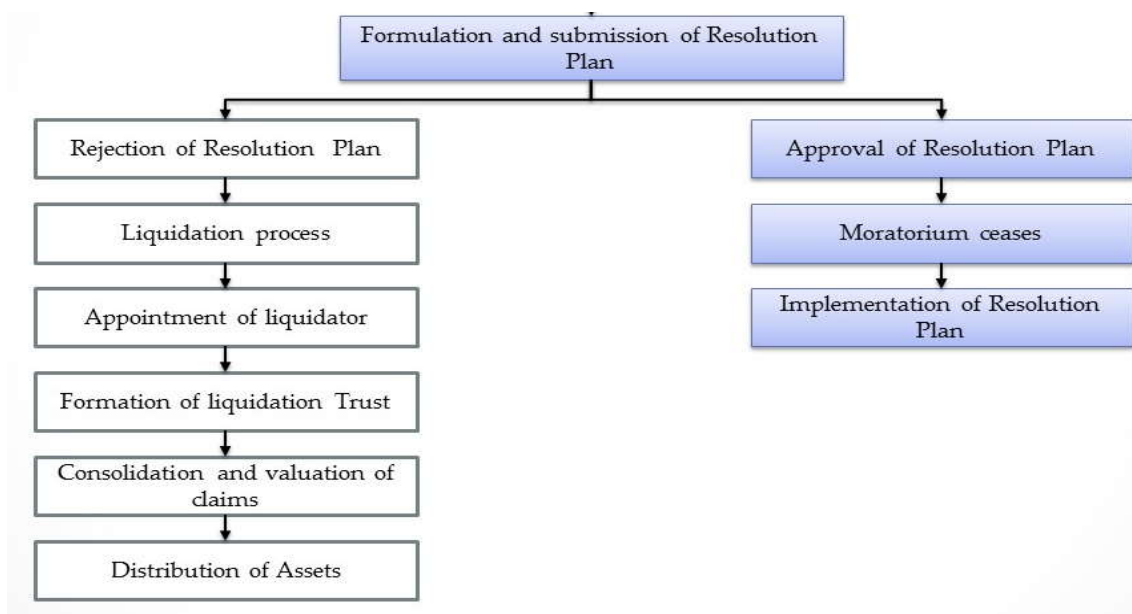
party of the corporate debtor solely on account of conversion or substitution of debt into equity shares or instruments convertible into equity shares, prior to the insolvency commencement date;

Explanation II.—For the purposes of this section, "**financial entity**" shall mean the following entities which meet such criteria or conditions as the Central Government may, in consultation with the financial sector regulator, notify in this behalf, namely:—

- (a) a scheduled bank;
- (b) any entity regulated by a foreign central bank or a securities market regulator or other financial sector regulator of a jurisdiction outside India which jurisdiction is compliant with the Financial Action Task Force Standards and is a signatory to the International Organisation of Securities Commissions Multilateral Memorandum of Understanding;
- (c) any investment vehicle, registered foreign institutional investor, registered foreign portfolio investor or a foreign venture capital investor, where the terms shall have the meaning assigned to them in regulation 2 of the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2017 made under the Foreign Exchange Management Act, 1999;
- (d) an asset reconstruction company registered with the Reserve Bank of India under section 3 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;
- (e) an Alternate Investment Fund registered with the Securities and Exchange Board of India;
- (f) such categories of persons as may be notified by the Central Government.

(XV) Resolution Plan

A resolution plan is defined under section 5(26) "means a plan proposed by resolution applicant for insolvency resolution of the corporate debtor as a going concern in accordance with Part II". It has to be approved by the CoC by a vote of not less than sixty-six per cent of voting share of the CoC members, before being presented to the Adjudicating Authority. The **sections 30 and 31 of the Code** deal with resolution plan. A resolution applicant may submit a resolution plan along with an affidavit stating that he is eligible under section 29A, to the resolution professional prepared on the basis of the information memorandum.



Duty of resolution professional on submission of Resolution plan: The resolution professional shall examine each resolution plan received by him to confirm that each resolution plan—

- (a) Provides the **manner for the payment of insolvency resolution process costs** in priority to the payment of other debts of the corporate debtor;
- (b) provides for the **payment of the debts of operational creditors** as may be specified by the Board which shall not be less than the amount to be paid to the operational creditors in the event of a liquidation of the corporate debtor under section 53; or the amount that would have been paid to such creditors, if the amount to be distributed under the resolution plan had been distributed in accordance with the order of priority in sub-section (1) of section 53

whichever is higher, and provides for the payment of debts of financial creditors, who do not vote in favour of the resolution plan, in such manner as may be specified by the Board, which shall not be less than the amount to be paid to such creditors in accordance with sub-section (1) of section 53 in the event of a liquidation of the corporate debtor.

Explanation 1. — For removal of doubts, it is hereby clarified that a distribution in accordance with the provisions of this clause shall be fair and equitable to such creditors.

Explanation 2. — For the purpose of this clause, it is hereby declared that on and from the date of commencement of the Insolvency and Bankruptcy Code (Amendment) Act, 2019, the provisions of this clause shall also apply to the corporate insolvency resolution process of a corporate debtor-

- i. where a resolution plan has not been approved or rejected by the Adjudicating Authority;
 - ii. where an appeal has been preferred under section 61 or section 62 or such an appeal is not time barred under any provision of law for the time being in force; or
 - iii. where a legal proceeding has been initiated in any court against the decision of the Adjudicating Authority in respect of a resolution plan;
- (c) provides for the management of the affairs of the Corporate Debtor after approval of the resolution plan;
- (d) the implementation and supervision of the resolution plan;
- (e) does not contravene any of the provisions of the law for the time being in force.
- (f) Conforms to such other requirements as may be specified by the Board.

Seeking approval of CoC: The resolution professional shall present such resolution plans, that satisfy the aforementioned conditions, to the committee of creditors for its approval by a vote of not less than sixty-six per cent of voting share of the financial creditors after considering its feasibility and viability, the manner of distribution proposed, which may take into account the order of priority amongst creditors as laid down in sub-section (1) of section 53, including the priority and value of the security interest of a secured creditor and such other requirements as may be specified by the Board. (Sec 30(3) and (4))

Provided that the committee of creditors shall not approve a resolution plan, submitted before the commencement of the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2017, where the resolution applicant is ineligible under section 29A and may require the resolution professional to invite a fresh resolution plan where no other resolution plan is available with it.

Provided further that where the resolution applicant referred to in the first proviso is ineligible under clause (c) of section 29A, the resolution applicant shall be allowed by the committee of creditors thirty days, to make payment of overdue amounts in accordance with the proviso to clause (c) of section 29A.

Provided also that nothing in the second proviso shall be construed as extension of period for the purposes of the proviso to section 12(3), and the corporate insolvency resolution process shall be completed within the period specified in that sub-section.

Provided also that the eligibility criteria in section 29A as amended by the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2018 shall apply to the resolution applicant who has not submitted resolution plan as on the date of commencement of the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2018.

Attending of meeting by resolution applicant: The resolution applicant may attend the meeting of the committee of creditors in which the resolution plan of the applicant is considered.

Provided that the resolution applicant shall not have a right to vote at the meeting of the committee of creditors unless such resolution applicant is also a financial creditor.

Voting on resolution plan: The committee of creditors shall-

- (a) evaluate the resolution plans as per evaluation matrix;
- (b) record its deliberations on the feasibility and viability of each resolution plan; and
- (c) vote on all such resolution plans simultaneously.

Where only one resolution plan is put to vote, it shall be considered approved if it receives requisite votes. Where two or more resolution plans are put to vote simultaneously, the resolution plan, which receives the highest votes, but not less than requisite votes, shall be considered as approved.

Provided that where two or more resolution plans receive equal votes, but not less than requisite votes, the committee shall approve any one of them, as per the tie-breaker formula announced before voting.

Provided further that where none of the resolution plans receives requisite votes, the committee shall again vote on the resolution plan that received the highest votes, subject to the timelines under the Code. (Reg 39(3B))

Submission of the resolution plan: The resolution professional shall submit the resolution plan as approved by the committee of creditors to the Adjudicating Authority. **[Section 30]**

Approval of resolution plan: If the Adjudicating Authority is satisfied that the resolution plan as approved by the committee of creditors meets the requirements as per section 30(2), it shall by order approve the resolution plan which shall be binding on the following:

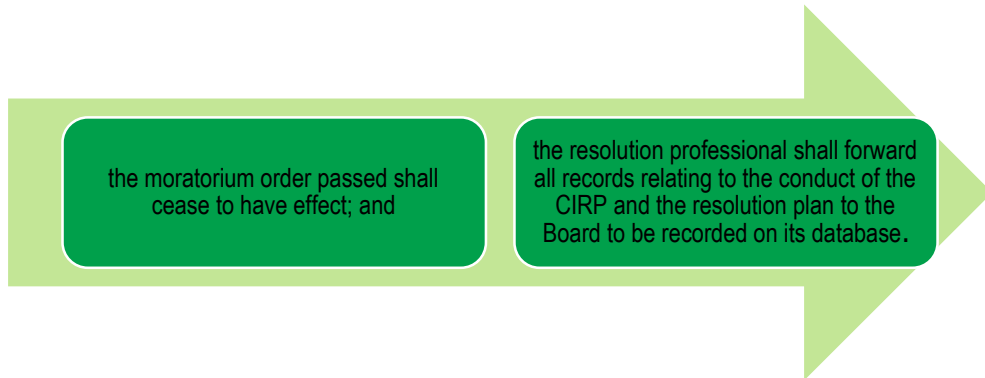
- corporate debtor and its employees,
- members, creditors, guarantors, and
- other stakeholders involved in the resolution plan
- Central Government, State Government and Local Authority

Case Law

SC in Committee of Creditors of *Essar Steel India Ltd. Vs. Satish Kumar Gupta & Ors.* Civil Appeal No. 8766-67 of 2019 dated 15th November 2019 it was decided that the successful resolution applicant does on a fresh slate, and all the liabilities get extinguished on approval of the resolution plan beyond what has been part of the plan.

Rejection of the resolution plan: Where the Adjudicating Authority is satisfied that the resolution plan does not conform to the above requirements, it may, by an order, reject the resolution plan.

Consequences of approval: After the order of approval,—



The resolution applicant shall obtain the necessary approval pursuant to the resolution plan approved, within a period of one year from the date of approval of the resolution plan by the Adjudicating Authority or within such period as provided for in such law, whichever is later.

Provided that where the resolution plan contains a provision for combination, as per section 5 of the Competition Act, 2002, the resolution applicant shall obtain the approval of the Competition Commission of India under that Act prior to the approval of such resolution plan by the committee of creditors. **[Section 31]**

Case Law

Supreme Court in the matter of *K. Sashidhar Vs. Indian Overseas Bank & Ors.* in Civil Appeal No. 10673 of 2018, C.A. No.10719 of 2018, 10971 of 2018 and SLP (C) No.29181 of 2018 dt 5 Feb 2019 it was decided that No provision has been envisaged by the legislature to empower the RP, the NCLT or NCLAT, to reverse the commercial decision of the CoC

Liabilities for previous offences:

(1) **Liability of a Corporate Debtor for an offence committed prior to the commencement of the corporate insolvency resolution process:** Notwithstanding anything to the contrary contained in this Code or any other law for the time being in force, the liability of a corporate debtor for an offence committed prior to the commencement of the corporate insolvency resolution process **shall cease**, and the corporate debtor shall not be prosecuted for such an offence from the date the resolution plan has been approved by the Adjudicating Authority under section 31, if the resolution plan results in the change in the management or control of the corporate debtor to a person who was not-

- a) a promoter or in the management or control of the corporate debtor or a related party of such a person; or
- b) a person with regard to whom the relevant investigating authority has, on the basis of material in its possession, reason to believe that he had abetted or conspired for the

commission of the offence, and has submitted or filed a report or a complaint to the relevant statutory authority or Court:

Provided that if a prosecution had been instituted during the corporate insolvency resolution process against such corporate debtor, it shall stand discharged from the date of approval of the resolution plan subject to requirements of this sub-section having fulfilled:

Provided further that every person who was a “designated partner” as defined in clause (j) of section 2 of the Limited Liability Partnership Act, 2008 or an “officer who is in default”, as defined in clause (60) of section 2 of the Companies Act, 2013, or was in any manner in-charge of, or responsible to the corporate debtor for the conduct of its business or associated with the corporate debtor in any manner and who was directly or indirectly involved in the commission of such offence as per the report submitted or complaint filed by the investigating authority, shall continue to be liable to be prosecuted and punished for such an offence committed by the corporate debtor notwithstanding that the corporate debtor’s liability has ceased under this sub-section.

(2) **When no action against the property of the corporate debtor shall be taken:** No action shall be taken against the property of the corporate debtor in relation to an offence committed prior to the commencement of the corporate insolvency resolution process of the corporate debtor, **where such property is covered under a resolution plan approved by the Adjudicating Authority under section 31**, which results in the change in control of the corporate debtor to a person, or sale of liquidation assets under the provisions of Chapter III of Part II of this Code to a person, who was not –

- (a) a promoter or in the management or control of the corporate debtor or a related party of such a person; or
- (b) a person with regard to whom the relevant investigating authority has, on the basis of material in its possession, reason to believe that he had abetted or conspired for the commission of the offence, and has submitted or filed a report or a complaint to the relevant statutory authority or Court

(3) Subject to the provisions contained in sub-sections (1) and (2), and notwithstanding the immunity given in this section, the corporate debtor and any person, who may be required to provide assistance under such law as may be applicable to such corporate debtor or person, shall extend all assistance and co-operation to any authority investigating an offence committed prior to the commencement of the corporate insolvency resolution process. [Section 32A]

Appeal against Approval of Resolution Plan: Any appeal from an order approving the resolution plan shall be in the manner and on the grounds laid down in sub-section (3) of section 61.

As per Section 61(3) of the Code, an appeal against an order of Adjudicating Authority for approving the resolution plan may be filed on the following grounds:-

- (a) The approved resolution plan is in contravention of the provisions of any law for the time being in force.
- (b) There has been material irregularity in exercise of the powers by the resolution professional during the corporate insolvency resolution period.
- (c) The debts owed to operational creditors of the corporate debtor have not been provided for in the resolution plan in the manner specified by the Board.
- (d) The insolvency resolution process costs have not been provided for repayment in priority to all other debts.
- (e) The resolution plan does not comply with any other criteria specified by the Board.

Consequences of non-submission of a Resolution Plan: When the Resolution Plan is not filed within 180 days of the Commencement date or such other extended period the Adjudicating Authority may pass orders for the liquidation of the corporate debtor.

Vide Circular No. IBBI/CIRP/41/2021, DATED 18-3-2021, under Regulation 40A of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 ('CIRP regulations') provides a model timeline for carrying out various activities envisaged in a corporate insolvency resolution process (CIRP).

Regulation 40B of the CIRP regulations require an interim resolution professional (IRP)/ resolution professional (RP) to file a set of forms (CIRP 1 to CIRP 6) within seven days of completion of specific activities to enable monitoring progress of CIRP. This implies that a Form (CIRP 1 to CIRP 6) would not be filed until the related activity is not completed for whatever reason. This makes monitoring of progress difficult. Regulation 40B of CIRP regulations require filing of Form CIRP 7 within three days of due date of completion of any activity stated in column (2) of the table below is delayed, and continue to file Form CIRP 7 every 30 days, until the said activity remains incomplete.

<i>Sl. No.</i>	<i>Activity requiring filing of Form CIRP 7, if not completed by the specified date</i>	<i>Timeline for filing Form CIRP 7 for the first time</i>	<i>Timeline for subsequent filing of Form CIRP 7</i>
<i>(1)</i>	<i>(2)</i>	<i>(3)</i>	<i>(4)</i>
<i>1</i>	<i>Public announcement is not made by T+3rd day</i>	<i>Date specified in column (2) + 3 days</i>	<i>X+30th day, X+60th day, X+90th day, and so on, till the activity is completed.</i>
<i>2</i>	<i>Appointment of RP is not made by T+30th day</i>		
<i>3</i>	<i>Information memorandum is not issued within 51 days</i>		

	<i>from the date of public announcement</i>		
4	<i>RFRP is not issued within 51 days from the date of issue of information memorandum</i>		
5	<i>CIRP is not completed by T+180th day</i>		

T = Insolvency commencement date, and

X = Date of filing of Form CIRP 7 for the first time under column (3).

This circular is applicable for all the processes ongoing as on the date of this circular.



4. LIQUIDATION PROCESS

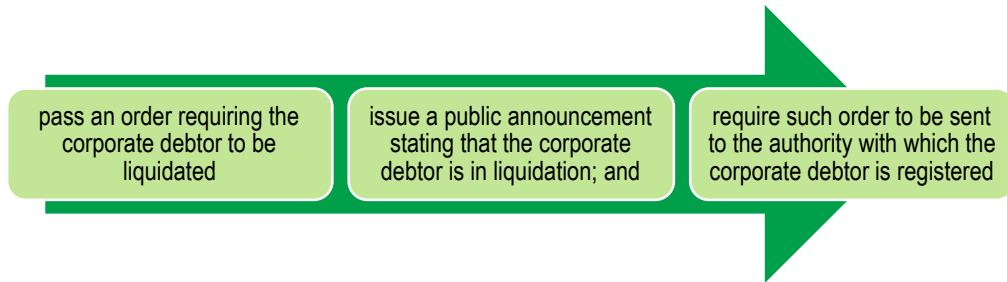
The Code concerns itself only with those corporate debtors which have defaulted in payment of debts. The corporate debtor, at the first stage, is put into resolution mode. The process is called the corporate insolvency resolution process. However, if attempts to resolve the insolvency of the corporate debtor fail, then only the liquidation provisions of the Code are triggered.

Where no plan is received during the CIRP period or where the plan presented is rejected by the Committee of Creditors or if the plan is not approved by the Adjudicating Authority, the Adjudicating Authority shall pass an order requiring the Corporate Debtor to be liquidated in the manner as laid down in Chapter III of the Act. CIRP always precedes Liquidation Process. There is no provision under the Code for direct Liquidation without undergoing CIRP.

Initiation of Liquidation process:

Section 33 of the Code provides that where the Adjudicating Authority, —

- (a) **Not received a Resolution plan:** Before the expiry of the insolvency resolution process period or the maximum period permitted for completion of the corporate insolvency resolution process or the fast track corporate insolvency resolution process, as the case may be, does not receive a resolution plan; or
- (b) **rejects the resolution plan** for the non-compliance of the requirements specified therein, it shall—



Intimation of the decision of the committee of creditors to liquidate to Adjudicating authority:

Where the resolution professional, at any time during the corporate insolvency resolution process but before confirmation of resolution plan, intimates the Adjudicating Authority of the decision of the committee of creditors approved by not less than sixty-six per cent of the voting share to liquidate the corporate debtor, the Adjudicating Authority shall pass a liquidation order.

Contravention of resolution plan as approved by the Adjudicating Authority: Where the resolution plan approved by the Adjudicating Authority under section 31 or under sub-section (1) of section 54L, is contravened by the concerned corporate debtor, any person other than the corporate debtor, whose interests are prejudicially affected by such contravention, may make an application to the Adjudicating Authority for a liquidation order.

Determination of contravention of the provisions of the resolution plan: On receipt of an application, if the Adjudicating Authority determines that the corporate debtor has contravened the provisions of the resolution plan, it shall pass a liquidation order.

Bar to filing of suits and legal proceedings: Subject to section 52, when a liquidation order has been passed, no suit or other legal proceeding shall be instituted by or against the corporate debtor. A suit or other legal proceeding may be instituted by the liquidator, on behalf of the corporate debtor, with the prior approval of the Adjudicating Authority.

Exception: Restrictions on filing of suits and legal proceedings shall not apply to legal proceedings in relation to such transactions as may be notified by the Central Government in consultation with any financial sector regulator.

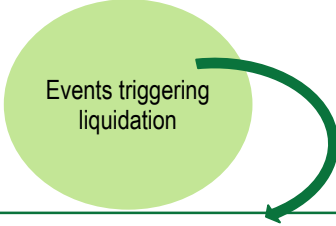
Order to be deemed to be notice of discharge: The order for liquidation under this section shall be deemed to be a notice of discharge to the officers, employees and workmen of the corporate debtor, except when the business of the corporate debtor is continued during the liquidation process by the liquidator.

So, from above it can be concluded that under the Code, a corporate debtor may be put into liquidation in the following scenarios:

- (i) Non-receipt of resolution plan during CIRP period;
- (ii) A 66% majority of the creditor's committee resolves to liquidate the corporate debtor at any time during the insolvency resolution process before confirmation of the resolution plan;

- (iii) The creditor's committee does not approve a resolution plan within 180 days (or within the extended 90 days);
- (iv) The NCLT rejects the resolution plan submitted to it on technical grounds; or
- (v) The debtor contravenes the agreed resolution plan and an affected person makes an application to the NCLT to liquidate the corporate debtor.

Once the NCLT passes an order of liquidation, a moratorium is imposed on the pending legal proceedings against the corporate debtor, and the assets of the debtor (including the proceeds of liquidation) vest in the liquidation estate.



Events triggering liquidation

- On rejection of resolution plan
- Adjudicating Authority does not receive a Resolution Plan on or before the expiry of the maximum time permitted for resolution
- Corporate debtor contravenes the Resolution Plan approved by AA, and any other person being prejudicially affected applies against such contravention
- Creditors' Committee decides to liquidate the corporate debtor at any time during insolvency process, before confirmation of any Resolution Plan

Case Law:

National Company Law Appellate Tribunal, New Delhi, in *Sreedhar Tripathy v. Gujarat State Financial Corporation*, 2022 gave the verdict that where corporate debtor was not functioning for last 19 years and all machinery had become scrap and CoC in its commercial wisdom decided to liquidate corporate debtor, impugned order passed by NCLT directing liquidation of corporate debtor was not to be interfered with.

In the given case, NCLT directed for liquidation of corporate debtor. Here Appellant challenged said order on ground that CoC never wanted to continue with CIRP and decision taken by CoC for liquidation of corporate debtor was not in its commercial wisdom. It was noted that corporate debtor was not functional and was completely shut for last 19 years.

It was held that CoC in its Legislative scheme has been empowered to take decision to liquidate corporate debtor, any time after its constitution and before confirmation of resolution plan. As corporate debtor had not been functioning for last 19 years and all machinery had become scrap, even buildings were in broken-down condition and CIRP would involve huge costs, decision taken by CoC to liquidate corporate debtor was not arbitrary and same was not open for Judicial review by NCLT.

TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. *An application under Section 9 of the Insolvency and Bankruptcy Code, 2016 was filed by the Raheja Portland Cement Limited in the capacity as operational creditor against the corporate debtor Makhija Builders and Developers Limited. The application was admitted by the order of the National Company Law Tribunal – Mumbai (NCLT, Mumbai) after giving a reasonable opportunity of being heard to Makhija Builders and Developers Limited and Mr. Ritesh was appointed as Interim Resolution Professional (IRP). However, Mr. Sanskar and Mr. Satvik, two of the directors of Makhija Builders and Developers Limited, were suspicious about the claims filed by Raheja Portland Cement Limited since they were much more than what was due to the company and therefore, they are desirous of making an appeal against the order of the NCLT, Mumbai. You, as a legal advisor, are required to advise them as to the maximum time within which an appeal against the order of the NCLT, Mumbai, can be filed by them with the National Company Law Appellate Tribunal (NCLAT).*
 - (a) *Mr. Sanskar and Mr. Satvik, the two directors of Makhija Builders and Developers Limited shall be able to prefer an appeal against the order passed by NCLT, Mumbai under Section 9 of the Insolvency and Bankruptcy Code, 2016, within a period of 45 days from the date of order.*
 - (b) *Mr. Sanskar and Mr. Satvik, the two directors of Makhija Builders and Developers Limited shall be able to prefer an appeal against the order passed by NCLT, Mumbai under Section 9 of the Insolvency and Bankruptcy Code, 2016, within a period of 30 days from the date of order.*
 - (c) *Mr. Sanskar and Mr. Satvik, the two directors of Makhija Builders and Developers Limited shall be able to prefer an appeal against the order passed by NCLT, Mumbai under Section 9 of the Insolvency and Bankruptcy Code, 2016, within a period of 15 days from the date of order.*
 - (d) *Mr. Sanskar and Mr. Satvik, the two directors of Makhija Builders and Developers Limited shall be able to prefer an appeal against the order passed by NCLT, Mumbai under Section 9 of the Insolvency and Bankruptcy Code, 2016, within a period of 10 days from the date of order.*
2. *Aakansha Plastics Limited, having registered office at Bhatinda, Punjab, was formed in the year 2005. On March 31, 2021, its paid-up share capital was ₹ 5,00,00,000; Amount due from Debtors viz. Shilpa Furnitures Private Limited and Shobhna Traders & Co. ₹ 4,00,00,000; Secured loans obtained from Crescent Bank Limited ₹ 6,00,00,000; Amount due to creditors, namely, Sambhav & Sons and Satyadev Suppliers Private Limited ₹ 3,00,00,000. The performance of the company decreased sharply due to stiff competition, wrong planning and*

mismanagement and it came on the verge of insolvency. Choose from the following alternatives as to who is the corporate debtor:

- (a) Shilpa Furnitures Private Limited and Shobhna Traders & Co.
 - (b) Aakansha Plastics Limited.
 - (c) Sambhav & Sons and Satyadev Suppliers Private Limited.
 - (d) Crescent Bank Limited.
3. *Ruby Petals Limited, a small company, files an application with the National Company Law Tribunal (NCLT) stating that the fast track corporate insolvency resolution process against it cannot be completed within the prescribed period of 90 days. On being satisfied, NCLT orders to extend the period of such process by 30 days. However, Ruby Petals Limited again initiates an application for further extension of time period of insolvency process by another 10 days. From the four options given below which one, do you think, is applicable in such a situation:*
- (a) *National Company Law Tribunal can extend the period of fast track corporate insolvency resolution process against Ruby Petals Limited by another 10 days since total extension does not exceed 45 days.*
 - (b) *National Company Law Tribunal can extend the period of fast track corporate insolvency resolution process against Ruby Petals Limited by another 10 days if the corporate debtor deposits ₹ 50,000 as penalty.*
 - (c) *National Company Law Tribunal can extend the period of fast track corporate insolvency resolution process against Ruby Petals Limited by another 10 days if the corporate debtor deposits ₹ 1,00,000 as penalty.*
 - (d) *National Company Law Tribunal cannot extend the period of fast track corporate insolvency resolution process against Ruby Petals Limited by another 10 days since such extension shall not be granted more than once.*
4. *Munikh Hospitality Services Limited was admitted in the Corporate Insolvency Resolution Process (CIRP) under Section 7 of the Insolvency and Bankruptcy Code. The Resolution Professional (RP) Mr. Somesh, after his appointment, conducted a meeting of Committee of Creditors (CoC) but the same was adjourned due to the lack of quorum. At the appointed date and time, when the adjourned meeting was resumed, a resolution was passed by the CoC members present, representing 51% of the voting rights, for liquidation of Munikh Hospitality Services Limited, the Corporate Debtor, before the completion of the Corporate Insolvency Resolution Process (CIRP). You, as a qualified Chartered Accountant comprising the team of RP, are required to advise whether the resolution of liquidation passed by certain members of CoC representing 51% of the voting rights is valid or not considering the applicable provisions of the Insolvency and Bankruptcy Code, 2016.*

- (a) *The resolution of liquidation of Munikh Hospitality Services Limited passed by certain members of CoC representing 51% of the voting rights is not valid since the resolution has not been approved by minimum of 90% of the voting shares of the creditors.*
 - (b) *The resolution of liquidation of Munikh Hospitality Services Limited passed by certain members of CoC representing 51% of the voting rights is not valid since the resolution has not been approved by minimum of 66% of the voting shares of the creditors.*
 - (c) *The resolution of liquidation of Munikh Hospitality Services Limited passed by certain members of CoC representing 51% of the voting rights is not valid since such resolution cannot be passed before the completion of the CIRP.*
 - (d) *The resolution of liquidation of Munikh Hospitality Services Limited passed by certain members of CoC representing 51% of the voting rights is valid since the same has been passed by the majority of creditors.*
5. *Shivdeep submitted his claim as an operational creditor to the liquidator of Chiranjeevi Food Products Limited which is under liquidation. After submission of his claim, Shivdeep is desirous of altering it. Out of the following four options, which one correctly indicates the time period within which he can alter his claim after its submission.*
- (a) *Shivdeep can alter his claim within five days of its submission to the liquidator of Chiranjeevi Food Products Limited.*
 - (b) *Shivdeep can alter his claim within ten days of its submission to the liquidator of Chiranjeevi Food Products Limited.*
 - (c) *Shivdeep can alter his claim within fourteen days of its submission to the liquidator of Chiranjeevi Food Products Limited.*
 - (d) *Shivdeep can alter his claim within thirty days of its submission to the liquidator of Chiranjeevi Food Products Limited.*

Descriptive Questions

1. *When will the provisions of insolvency and liquidation be applicable to a corporate person?*
2. *What is the Insolvency Resolution Process for financial creditors?*
3. *What is the Insolvency Resolution Process for operational creditors?*
4. *What are the eligibility criteria for appointment of an Insolvency Professional as a Resolution Professional for a corporate insolvency resolution process?*
5. *What is the procedure of Insolvency Resolution Process for a Corporate Applicant?*
6. *Is there any time limit for completion of the Insolvency Resolution Process?*
7. *What is the effect of order of moratorium?*

8. What is a Resolution plan?
9. What is the significance of the Corporate Insolvency Resolution Commencement Date?
10. Mr. Ram, an operational creditor filed an application for corporate insolvency resolution process. He did not propose for the appointment of an interim resolution professional in the application. State the provisions given by the Code to resolve such a scenario including the term of IRP so appointed.

ANSWERS

Answer to Multiple Choice Questions

1.	b	2.	b	3.	d	4.	b	5.	c

Answer to Descriptive Answers

1. The provisions relating to the insolvency and liquidation of corporate debtors shall be applicable only when the amount of the default is one lakh rupees or more. However, the Central Government may, by notification, specify the minimum amount of default of higher value which shall not be more than one crore rupees.

Vide Notification No. S.O.1205(E), date 24-03-22, minimum amount of default is increase to 1 crore for triggering CIRP under the IBC.

2. A financial creditor either itself or along with other financial creditors may lodge an application before the Adjudicating Authority (National Company Law Tribunal) for initiating corporate insolvency resolution process against a corporate debtor who commits a default in payment of its dues.

The financial creditor shall along with the application give evidence in support of the default committed by the corporate debtor. He shall also give the name of the interim resolution professional.

Where the Adjudicating Authority is satisfied that a default has occurred and the application by the financial creditor is complete and there are no disciplinary proceedings pending against the proposed resolution professional, it may admit such application made by the financial creditor.

If the Adjudicating Authority is satisfied that default has not occurred (reasons to be recorded in writing) or the application is incomplete or any disciplinary proceeding is pending against the resolution professional, it shall reject the application. However, the applicant may rectify the defect within seven days of receipt of notice of rejection from the Adjudicating Authority.

3. On the occurrence of default, an operational creditor shall first send a demand notice and a copy of invoice to the corporate debtor.

The corporate debtor shall within a period of ten days of receipt of demand notice notify the operational creditor about the existence of a dispute, if there is any and record of pendency of any suit or arbitration proceedings. He shall also provide the details of repayment of unpaid operational debt in case the debt has or is being paid.

After the expiry of ten days, if the operational creditor does not receive his payment or the confirmation of a dispute that existed even before the demand notice was sent, he may file an application before the Adjudicating Authority for initiating a corporate insolvency resolution process.

The Adjudicating Authority shall within fourteen days of receipt of the application, admit or reject the application. However, before rejecting the application, an opportunity shall be given to the applicant to rectify the defect within seven days of receipt of rejection.

4. As per Regulation 3 of Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016, an insolvency professional shall be eligible for appointment as a resolution professional for a corporate insolvency resolution process if he and all partners and directors of the insolvency professional entity of which he is partner or director are independent of the corporate debtor i.e.,

- He is eligible to be appointed as an independent director on the board of the corporate debtor under Section 149 of the Companies Act, 2013, where the corporate debtor is a company.
- He is not a related party of the corporate debtor.
- He is not an employee or proprietor or a partner of a firm of auditors or secretarial auditors in practice or cost auditors of the corporate debtor in the **last three financial years**.
- He is not an employee or proprietor or a partner of a legal or consulting firm that has or had any transaction with the corporate debtor amounting to **five per cent** or more of the gross turnover of such firm in the **last three financial years**.

5. Where a corporate debtor has committed a default, a corporate applicant thereof may file an application for initiating corporate insolvency resolution process with the Adjudicating Authority.

The corporate applicant shall furnish the information relating to books of account and other documents and a resolution professional shall be appointed as interim resolution professional.

The Adjudicating Authority may either accept or reject the application within fourteen days of receipt of application. However, applicant shall be allowed to rectify the defect within seven days of receipt of notice of such rejection.

6. Section 12 states that any Insolvency Resolution Process shall be completed within a period of one hundred and eighty days from the date of admission of the application to initiate the process.

However, the National Company Law Tribunal (NCLT) may on an application made by the resolution professional, under a resolution passed by the Committee of Creditors, by a vote of 66% of voting shares, after consideration provide one extension which shall not extend more than 90 days.

Second proviso to Section 12 (3) states that the corporate insolvency resolution process (CIRP) shall compulsorily be completed within **330 days** from the insolvency commencement date including any extension of the time period of corporate insolvency resolution process granted under Section 12 and also the time taken in legal proceedings in relation to such resolution process of the corporate debtor.

7. Section 14 contains the provisions relating to moratorium. During the moratorium period the following acts shall be prohibited:
- (a) The institution of suits or continuation of any pending suits or proceedings against the corporate debtor including execution of any judgment, decree or order in any court of law, tribunal, arbitration panel or other authority;
 - (b) Transferring, encumbering, alienating or disposing of by the corporate debtor any of its assets or any legal right or beneficial interest therein;
 - (c) Any action to foreclose, recover or enforce any security interest created by the corporate debtor in respect of its property including any action under the SARFAESI Act, 2002
 - (d) The recovery of any property by an owner or lessor where such property is occupied by or in the possession of the corporate debtor.

Explanation to Section 14 (1) clarifies that notwithstanding anything contained in any other law for the time being in force, a licence, permit, registration, quota, concession, clearance or a similar grant or right given by the Central Government, State Government, local authority, sectoral regulator or any other authority constituted under any other law for the time being in force, **shall not be suspended or terminated on the grounds of insolvency**, subject to the condition that there is no default in payment of current dues arising for the use or continuation of the license or a similar grant or right during moratorium period.

8. According to Section 5 (26), a 'resolution plan' means a plan proposed by resolution applicant for insolvency resolution of the corporate debtor as a going concern in accordance with Part II of the Code.

Explanation to Section 5 (26) clarifies that a resolution plan may include provisions for the restructuring of the corporate debtor, including by way of merger, amalgamation and demerger.

The aim of the Code is to revive the corporate debtor and therefore, resolution plan should be such that it is capable of resolving the insolvency of the corporate debtor as a going concern.

As per Section 30, the resolution applicant shall prepare resolution plan on the basis of information memorandum and submit the same to the resolution professional.

Each Resolution Plan shall be examined by the resolution professional to confirm that each such plan:

- (i) provides for payment of insolvency resolution costs;
- (ii) provides for repayment of the debts to operational creditors;
- (iii) provides for management of affairs of the company after approval of the resolution plan;
- (iv) provides for implementation and supervision of the resolution plan;
- (v) does not contravene provisions of the law for the time being in force; and
- (vi) conforms to such other requirement as may be specified by the Board.

The resolution plan needs to be submitted within the prescribed time as provided by Section 12. The prescribed time limit is 180 days and in case of extension it is 270 days. Further, 330 days have also been mandated which shall include any extension of the time period of corporate insolvency resolution process granted under Section 12 and also the time taken in legal proceedings in relation to such resolution process of the corporate debtor.

In case of Fast Track Resolution, the time limit is 90 days and if extension is required, another 45 days can be granted.

The resolution professional shall submit the resolution plan to the committee of creditors for its approval which may approve the plan by a vote of not less than 66% of voting share of the financial creditors. Operational creditors have no say in approving the resolution plan.

The resolution professional shall submit the approved plan to the Adjudicating Authority.

9. The commencement date of the corporate insolvency resolution is the beginning of moratorium or a calm period till the completion of the corporate insolvency resolution process during which all suits and legal proceedings etc. against the Corporate Debtor are held in abeyance to give time to the entity to resolve its status.
10. **Appointment of IRP:** As per Section 16 of the Code where the application for corporate insolvency resolution process is made by an operational creditor and no proposal for an interim resolution professional is made in the said application, the Adjudicating Authority shall make a reference to the Board (IBBI) for the recommendation of an insolvency professional who may act as an interim resolution professional.

The Board (IBBI) shall recommend the name of an insolvency professional to the Adjudicating Authority against whom no disciplinary proceedings are pending, within ten days of the receipt of a reference from the Adjudicating Authority.

Period of appointment of IRP: the term of the Interim Resolution Professional shall continue from his appointment till the date of appointment of the Resolution Professional by COC in its first meeting under Section 22 of the Code.

[illegible]

CHAPTER

3

THE INSOLVENCY AND BANKRUPTCY CODE, 2016



LEARNING OUTCOMES

At the end of this Chapter, you will be able to:

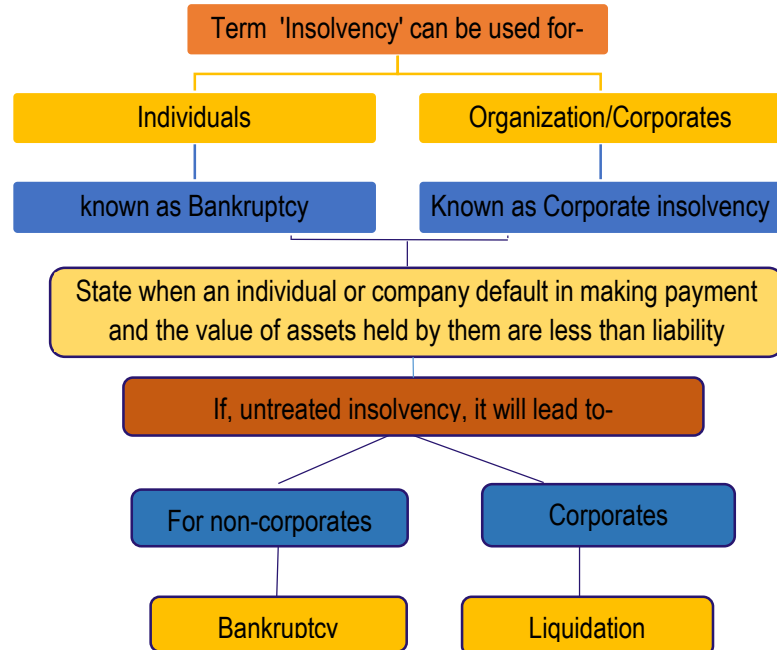
- ☐ Explain the concepts of Insolvency and Bankruptcy Code, 2016 (Code)
- ☐ Explain the relationship between Bankruptcy, Insolvency and Liquidation
- ☐ Explain the important terminologies used in the Code.
- ☐ Identify the structure and applicability of the Code.
- ☐ Elaborate the manner and process of Insolvency Resolution Process for Corporate Persons



1. INTRODUCTION

Concept of Insolvency and Bankruptcy

- The term insolvency is used for both individuals and organizations. Insolvency is when there is a default in payment and it's not paid. Default is defined under section 3(12) of the Insolvency and Bankruptcy Code, 2016. Untreated insolvency will lead to bankruptcy for non-corporates and liquidation of corporates. Creditors put money into debt investments today in return for the promise of fixed future cash flows. But the returns expected on these investments are still uncertain because at the time of repayment, the corporate or individual (debtor) may make repayments as promised, or he may default and does not make the payment. When default happens in payment, the debtor is considered insolvent. The debtor may be insolvent because of:
 - Financial Failure:** a persistent mismatch between payments by the enterprise and receivables into the enterprise, even though the business model is generating revenues, or
 - Business Failure:** which is a breakdown in the business model of the enterprise, and it is unable to generate sufficient revenues to meet payments¹ or there may be avoidance of transaction because of which also insolvency may have happened.



¹ The Report of the Bankruptcy Law Reforms Committee Volume I: Rationale and Design, November 2015

- From the above it is evident that insolvency is a state and bankruptcy is a conclusion. A bankrupt would be a conclusive insolvent whereas all insolvencies will not lead to bankruptcies. Insolvency situation can be resolved through resolution mechanism under the Code and a failed resolution mechanism would lead to liquidation process in relation to corporates and bankruptcy process in relation to individuals under the Code.
- **Avoidance Transactions:** It is covered in Chapter III of IBC, 2016. The relevant provisions are in the following Sections
 - Preferential Transactions (Sec 43 and 44)
 - Undervalued Transactions (Sec 45 to Sec 48)
 - Transactions Defrauding Creditors (Sec 49)
 - Extortionate Credit Transactions (Sec 50 and Sec 51)
 - There is also Provisions for Fraudulent Trading or wrongful Trading (Sec 66 and Sec 67)

The IRP/ RP/ Liquidator has to form an opinion, then determine the avoidance transactions and thereafter file the petition before Hon'ble NCLT under the above provisions against the perpetrators. There are timelines prescribed for the all the activities under Regulations. However the times are not mandatory as per NCLAT.

Case Law

NCLAT in the matter of *Prasant Chandra Rath (Suspended Director of Corporate Debtor) Vs. Surya Kanta Satapathy (RP) Company Appeal (AT) (Insolvency) No. 850 of 2022 and Company Appeal (AT) (Insolvency) No. 869 of 2022* in order dated 30th Sept 2022 has decided that CIRP Regulations 35-A is not mandatory and the requirement for approaching the Adjudicating Authority for appropriate relief on or before 135th day of the Insolvency Commencement Date is only directory.

Relationship between Bankruptcy, Insolvency & Liquidation

In lucid language, if any person or entity is unable to pay off the debts and it owes, to their creditor, on time or as and when they became due and payable, and if defaults then such person or entity is regarded as "insolvent".

Bankruptcy is a legal proceeding involving a person or business that is unable to repay outstanding debts. The bankruptcy process begins with a petition filed by the debtor, or by the creditors. All of the debtor's assets are measured and evaluated, and the assets may be used to repay a portion of outstanding debt.

Liquidation is the winding up of a corporation or incorporated entity. There are many persons that can initiate proceedings to cause the Liquidation, those being:-

- The Regulatory Bodies;
- The Directors of a Company;

- The Shareholders of a Company; and
- An Unpaid Creditor of a Company

In nut shell, **insolvency** is common to both bankruptcy and liquidation. Not being able to pay debts as and when they became due and payable are the leading cause of Liquidation and is the only way that can cause a natural person to become a bankrupt.

Objectives: A sound legal framework of Insolvency law was required for achieving the following objectives:-

- **Improved handling of conflicts between creditors and the debtor:** It can provide procedural certainty about the process of negotiation, in such a way as to reduce problems of common property and reduce information asymmetry for all economic participants.
- **Avoid destruction of value:** It can also provide flexibility for parties to arrive at the most efficient solution to maximise value during negotiations. The Insolvency law will create a platform for negotiation between creditors and external investors which can create the possibility of such rearrangements.
- **Drawing the line between malfeasance and business failure:**
 - (a) If malfeasance then promoters should be held responsible
 - (b) If business fails then, the company should move forward for its resolution.

The recommendations of the Bankruptcy Law Reforms Committee (BLRC) led to the enactment of the Insolvency and Bankruptcy Code, 2016 ("IBC or code") on May 28, 2016.

The IBC, consolidating all existing insolvency-related laws, has brought about a revolutionary change in the form of a robust, modern and sophisticated insolvency framework. This framework seeks to achieve a resolution for corporate debtors in distress and failing that, their liquidation in a time bound manner. Prior to the IBC, the legislative framework for insolvency and restructuring was fragmented across multiple legislations, such as the Companies Act 2013, the Sick Industrial Companies (Special Provisions) Act, 1985, Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, the Recovery of Debts due to Banks and Financial Institutions Act (RDDBFI Act), 1993, the Presidency Towns Insolvency Act, 1909, the Provincial Insolvency Act, 1920.

Preamble of the Code

Objectives of the Code are given in the Preamble.

An Act to-

- Consolidate and amend the laws relating to reorganisation and insolvency resolution of corporate persons, partnership firms and individuals;
- In a time bound manner for maximisation of value of assets of such persons, - to promote entrepreneurship;

- Availability of credit;
- Balance the interests of all the stakeholders including alteration in the order of priority of payment of Government dues;
- To establish an Insolvency and Bankruptcy Board of India; and
- For matters connected therewith or incidental thereto.

IBC is not a recovery mechanism

As per preamble the objective of IBC is resolution of the corporate debtor and it cannot be used as a recovery mechanism.

Case Laws

NCLAT in the Company Appeal (AT) (Insolvency) No. 540 of 2020 dt 17th Jan 2022, in the matter of *M/s Amsons Communication Pvt. Ltd. Vs. M/s ATS Estates Pvt. Ltd.* has ordered that the provisions of Code cannot be allowed as a recovery mechanism or to recover the claim of interest by Operational Creditor.

Structure of the Code

The Code is structured into 5 parts comprising of 255 sections and 12 Schedules. Each part deals with a distinct aspect of the insolvency resolution process.

Part	Part Content	Chapters and Sections	Chapter / Contents
I	Preliminary	(1-3) Part I	1. Short title, extent & Commencement 2. Application 3. Definitions
II	Insolvency Resolutions and Liquidation for Corporate Persons	(4 – 77) Part II	1. Preliminary (Application & Definitions) 2. Corporate Insolvency Resolution Process 3. Liquidation Process 4. Pre-Packaged Insolvency Resolution Process 5. Fast Track Corporate Insolvency Resolution Process 6. Voluntary Liquidation of Corporate Persons 7. Adjudicating Authority for Corporate Persons 8. Offences & Penalties
III	Insolvency Resolution and Bankruptcy for Individuals and	(78 - 187) Part III	1. Preliminary (Application & Definitions) 2. Fresh Start Process 3. Insolvency Resolution Process 4. Bankruptcy Order for Individuals & Partnership

	Partnership Firms		Firms 5. Administration & Distribution of the Estate of the Bankrupt 6. Adjudicating Authority 7. Offences & Penalties
IV	Regulation of Insolvency Professionals, Agencies and Information Utilities	(188 – 223) Part IV	1. The Insolvency and Bankruptcy Board of India 2. Powers & Functions of the Board 3. Insolvency Professional Agencies 4. Insolvency Professionals 5. Information Utilities 6. Inspection & Investigation 7. Finance, Accounts & Audit
V	Miscellaneous	(224 – 255) Part V	Miscellaneous
	Schedules I to XII		

An **Insolvency and Bankruptcy Board of India (IBBI)** is established to administer the work of insolvency and bankruptcy of corporate persons, firms and individuals. IBBI is the regulator who regulates the main components of IBC ecosystem, i.e, Insolvency Professional Agencies (IPAs), Insolvency Professionals (IPs), Registered Valuers (RVs) and Information Utilities (IUs). IPA is the second limb of regulator.

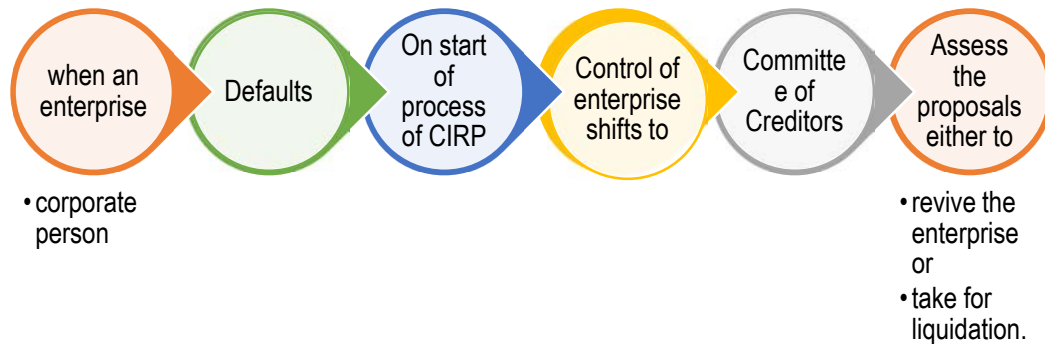
Foundation of Code

A key innovation of the IBC is a four-pillar institutional framework, comprising (a) the **first pillar**: the judicial Adjudicating Authority, being the National Company Law Tribunal (NCLT or Adjudicating Authority) where corporate insolvency matters shall be heard & NCLAT will be Appellate Authority; (b) the **second pillar**: the regulator, being Insolvency and Bankruptcy Board of India (IBBI) which has regulatory oversight over insolvency professionals and insolvency professional agencies (IPA); (c) the **third pillar**: a class of regulated persons, being the insolvency professionals who play a key role in the efficient working of the insolvency and bankruptcy process under the IBC; and, (d) the **fourth pillar**: a new industry called information utilities (IU) to electronically store facts about lenders and terms of lending.

Initiation of Corporate Insolvency Resolution Process (“CIRP”)

CIRP proceedings may be initiated against a corporate debtor by the corporate debtor itself or any of its financial creditor or operational creditor. When the Code was enacted, the minimum amount of default to initiate CIRP against a corporate debtor was INR One Lakh. However, the Central Government has by notification dated 24th March 2020 raised the threshold value of minimum amount of default to one crore rupees.

The detailed procedure for initiation of CIRP by stakeholders is described as follows:



Decisions are required to be taken in a time bound manner so that there are greater chances that the enterprise is saved as a going concern and productive resources of economy can be put to best use. The CIRP commences from the date of admission of an application filed for its initiation. The process entails a moratorium where a calm period is imposed and there is stay on suit or proceedings against the corporate debtor to give the debtor a better chance to revive and continue as a going concern. The moratorium period is 180 days and in limited circumstances, if the CoC, with a 66% majority, decides that the complexity of the case requires more time for a resolution plan to be finalized, a one-time extension of up to 90 days may be granted with prior approval of the NCLT.

The CIRP shall mandatorily be completed within a period of 330 days from the insolvency commencement date, including any extension and the time taken in legal proceedings in relation to the resolution process of the corporate debtor. The said amendment has been undertaken to ensure a timely resolution in view of the fact that the 270 day deadline was being breached on account of legal proceedings against the corporate debtor.

Provisions relating to Corporate Insolvency Resolution Process (section 4 to section 32 of the Code) will be applicable.

Provisions relating to Liquidation Process of Corporates (section 33 to section 54 of the Code) will be applicable in case where the enterprise is undergoing liquidation.

Provisions relating to Fast Track Corporate Insolvency Resolution Process of Small Corporate Persons (section 55 to section 58 of Insolvency Code) will be applicable in case where the enterprise is a small company as per Companies Act, 2013 or a start-up or an unlisted company with total assets not exceeding rupees one crore.

Provisions relating to Voluntary Liquidation (section 59 of the Code) will be applicable to corporate person who intends to liquidate itself voluntarily and has not committed any default.

Winding up of companies - In most of the cases, winding up of companies will be through the Liquidation Process under the Code only.

Bankruptcy of individuals and firms - Part III of Insolvency Code 2016 (containing sections 78-187) deals with insolvency resolution and bankruptcy for individuals and partnership firms. This Part shall apply to matters relating to fresh start, insolvency and bankruptcy of individuals and partnership firms. Debt Recovery Tribunal (DRT) will be the Adjudicating Authority and Debt Recovery Appellate Tribunal (DRAT) will be the Appellate Authority for individuals and firms. These provisions are not yet effective except for the provisions pertaining to personal guarantors to corporate debtors in which case the NCLT will be the Adjudicating Authority and NCLAT will be Appellate Authority, if the process is going on or otherwise DRT/ DRAT.

Flow of insolvency resolution process for individuals-

- The process will be managed by 'resolution professional' under the direction of 'Adjudicating Authority'.
- Insolvency Resolution Process will be initiated.
- Finalise 'repayment plan' with concurrence of debtor and committee of creditors.
- Upon consensus on repayment plan the individual or firm will get a discharge order.
- On failure to finalize the repayment plan, the creditors/debtor can file an application for 'bankruptcy' and the Adjudicating Authority may pass the bankruptcy order.
- The resolution professional who is a bankruptcy trustee will take over estate of the bankrupt. He will sell or dispose it off and satisfy payments of creditors to the extent possible.
- After that, the bankrupt will get a 'discharge order'.
- The discharge order will be registered with Board (IBBI) in a register referred to in section 196 of the Code.

Provisions of this Code to override other laws: Section 238 of the Code states that the Code shall have overriding effect over other laws.

For example, sections 53 and 178 of Insolvency and Bankruptcy Code, 2016 provide that distribution from sale of assets will be as specified in that section, notwithstanding anything to the contrary contained in any other law enacted by the Parliament or any State Legislature for the time being in force.

Many tax laws (including GST) also provide for first charge on assets of the taxable person. However, with the overriding effect of Section 238, distribution from sale of assets in Liquidation Process or payment as per the resolution plan in CIRP under the Code, will prevail over other laws.

Extent and Commencement of the Code:

As per section 1 of the Insolvency and Bankruptcy Code, it extends to the whole of India.

This Code came into enforcement on 28th May 2016, however, the Central Government appointed different dates for different provisions of this Code.

Significant amendments: The Code has been first amended by the Insolvency and Bankruptcy (Amendment) Ordinance, 2017, passed on November 23, 2017. This Ordinance became an Act on January 18, 2018. It was known as the Insolvency and Bankruptcy Code (Amendment) Act, 2018. It was made applicable from November 23, 2017.

The second amendment was made vide the **Insolvency and Bankruptcy Code (Amendment) Ordinance, 2018, on June 6, 2018**. Further, the said ordinance, in the form of the Insolvency and Bankruptcy (Second Amendment) Bill received the assent of the President on the 17th August, 2018 and thus the **Insolvency and Bankruptcy Code (Second Amendment) Act, 2018** was enacted.

The third amendment was made vide the **Insolvency and Bankruptcy Code (Amendment) Bill, 2019** which received the assent of the President on 5th August, 2019 and thus the **Insolvency and Bankruptcy Code (Amendment) Act, 2019** was promulgated.

The fourth amendment was made vide the **Insolvency and Bankruptcy Code (Amendment) Ordinance, 2019, on December 28, 2019**. Further, the said ordinance, in the form of the Insolvency and Bankruptcy (Amendment) Bill, 2020 received the assent of the President on the 13th March, 2020 and thus the **Insolvency and Bankruptcy Code (Amendment) Act, 2020** was enacted.

Due to the advent of COVID-19 pandemic, the IBC was amended by insertion of Section 10A to suspend the initiation of CIRP under Sections 7, 9 and 10 of the IBC for any default arising on or after March 25, 2020.

The Code has undergone significant amendments since its enactment-

- to keep up with the developments and demands of the economy
- for effective implementation of law
- to remove the bottlenecks

To achieve desired objectives of the Code, the President promulgated the 'Insolvency and Bankruptcy Code (Amendment) Ordinance, 2021 on 4th April 2021. The Ministry of Law and Justice on 12th of August 2021 enacted the Insolvency and Bankruptcy Code (Amendment) Act, 2021 w.r.e.f from 4th day of April, 2021.

The amendments was made with an intent to provide an efficient alternative insolvency resolution framework for corporate persons classified as micro, small and medium enterprises (MSMEs) under the Code, for ensuring quicker, cost-effective and value maximizing outcomes for all the stakeholders, in a manner which is least disruptive to the continuity of MSMEs businesses and which preserves jobs. By this amendment the Provisions related to PPIRP and MSMEs was introduced.

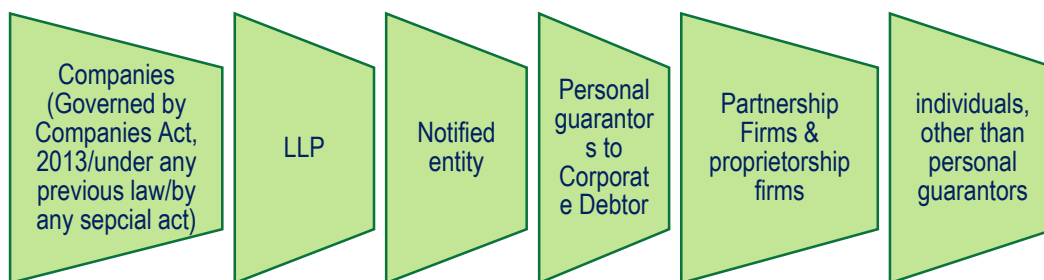
It provides an efficient alternative insolvency resolution framework for corporate persons classified as MSMEs for timely, efficient & cost-effective resolution of distress thereby ensuring positive signal to debt market, employment preservation, ease of doing business and preservation of enterprise

capital. Other expected impact and benefits of the amendment in Code are lesser burden on Adjudicating Authority, assured continuity of business operations for corporate debtor (CD), less process costs & maximum assets realization for financial creditors (FC) and assurance of continued business relation with CD and rights protection for operational Creditors (OC).

Applicability of the Code [Section 2]

The provisions of the Code shall apply for insolvency, liquidation, voluntary liquidation or bankruptcy of the following entities:-

- (a) Any company incorporated under the Companies Act, 2013 or under any previous law.
- (b) Any other company governed by any special act for the time being in force, except in so far as the said provision is inconsistent with the provisions of such Special Act.
- (c) Any Limited Liability Partnership under the LLP Act 2008.
- (d) Any other body incorporated under any law for the time being in force, as the Central Government may by notification specify in this behalf.
- (e) ²Personal guarantors to corporate debtors (CD);
- (f) Partnership firms and proprietorship firms; and
- (g) Individuals, other than persons referred to in clause (e)



Case Law

SC in *Lalit Kumar Jain v. Union of India*, in 2021 held with respect to the “Application of Code” that there is sufficient indication in Code by sections 2(e), 5(22), sections 60 and 179 indicating that personal guarantors, though forming part of larger grouping of individuals, are to be, in view of their intrinsic connection with corporate debtors, dealt with differently, through same adjudicatory process and by same forum as such corporate debtors.

² Personal guarantors of corporate debtors have been treated as a separate class. The application for bankruptcy of individual personal guarantor will have to be filed before NCLT as per section 60(2) of the IBC, 2016. Insolvency Code has been made applicable to personal guarantors of corporates w.e.f. 23-11-2017

Notification No. S.O. 4126 (E), dated 15-11-2019 making provisions of IBC applicable in respect of 'personal guarantors to corporate debtors' as another category of persons is valid. Even the approval of a resolution plan does not ipso facto discharge a personal guarantor (of a corporate debtor) of her or his liabilities under contract of guarantee.

Non-applicability of the Code: The Code is not applicable to corporates in finance sector. Section 3(7) of Insolvency & Bankruptcy Code, 2016 states that "Corporate person" shall not include any financial service provider.

"Financial service provider" means a person engaged in the business of providing financial services in terms of authorisation issued or registration granted by a financial sector regulator [section 3(17)].

However, section 227 of the Code, which was notified on 1-5-2018 provided that, Central Government can notify financial service providers for purpose of insolvency and liquidation proceedings, which may be conducted under the Insolvency & Bankruptcy Code, in consultation with appropriate financial sector regulator. As per notification dated 18-11-2019 it has been notified by the central government that insolvency resolution and liquidation proceedings of non-banking finance companies (which include housing finance companies) with asset size of Rs.500 crore or more, as per last audited balance sheet, shall be undertaken in accordance with the provisions of the Code and Rules made thereunder.

Case Laws

National Company Law Tribunal, Mumbai Bench, in 2022 decided in the *State Co-operative Bank Ltd. v. Shri Siddheshwar Sahakari Sakhar Karkhana Ltd.* that corporate debtor being a co-operative society was not a corporate person to whom provision of Code were applicable. Here as corporate debtor was registered/incorporated under Multi-State Co-operative Societies Act, 2002, which provides specific statutes for winding up of societies registered under same, and hence corporate debtor could not be put under insolvency resolution process.



2. IMPORTANT DEFINITIONS [SECTIONS 3 AND 5]

- (1) **Board** means the Insolvency and Bankruptcy Board of India (IBBI) established under section 188(1) of the Code [Section 3(1)].

The Board shall be a body corporate by the name aforesaid, having perpetual succession and a common seal, with power, subject to the provisions of this Code, to acquire, hold and dispose of property, both movable and immovable, and to contract, and shall, by the said name, sue or be sued [Section 188(2)].

The board will have powers of civil court as to the issue of summons, discovery and production of books, inspection of books/registers and issue of commissions for examination of witnesses [Section 196(3) of the Code]

- (2) **Charge** means an interest or lien created on the property or assets of any person or any of its undertakings or both, as the case may be, as security and includes a mortgage; [Section 3(4)]
- (3) **Claim** means:
- (a) **a right to payment**, whether or not such right is reduced to judgment, fixed, disputed, undisputed, legal, equitable, secured, or unsecured;
 - (b) **right to remedy for breach of contract** under any law for the time being in force, if such breach gives rise to a right to payment, whether or not such right is reduced to judgment, fixed, matured, unmatured, disputed, undisputed, secured or unsecured; [Section 3(6)]
- (4) **Corporate Person** means :
- (a) a company as defined under section 2(20) of the Companies Act, 2013;
 - (b) a Limited Liability Partnership as defined in 2(1)(n) of Limited Liability Act, 2008; or,
 - (c) any other person incorporated with limited liability under any law for the time being in force but shall not include any financial service provider. [Section 3(7)]
- (5) **Corporate Debtor** means a corporate person who owes a debt to any person. [Section 3(8)]
- (6) **Creditor** means any person to whom a debt is owed and includes –
- a financial creditor,
 - an operational creditor,
 - a secured creditor,
 - an unsecured creditor, and
 - a decree holder. [Section 3(10)]
- (7) **Debt** means a liability or obligation in respect of a claim which is due from any person and includes a financial debt and operational debt. [Section 3(11)]

Financial Debt - "Financial debt" means a debt along with interest, if any, which is disbursed against the consideration for the time value of money and includes—

- (a) money borrowed against the payment of interest.
- (b) any amount raised by acceptance under any acceptance credit facility or its dematerialised equivalent.
- (c) any amount raised pursuant to any note purchase facility or the issue of bonds, notes, debentures, loan stock or any similar instrument.

- (d) the amount of any liability in respect of any lease or hire purchase contract which is deemed as a finance or capital lease under the Indian Accounting Standards or such other accounting standards as may be prescribed.
- (e) receivables sold or discounted other than any receivables sold on non-recourse basis.
- (f) any amount raised under any other transaction, including any forward sale or purchase agreement, having the commercial effect of a borrowing.

Explanation.— For the purposes of this sub-clause - (i) any amount raised from an allottee under a real estate project shall be deemed to be an amount having the commercial effect of a borrowing; and (ii) the expressions, "allottee" and "real estate project" shall have the meanings respectively assigned to them in section 2(d) and 2(zn) of the Real Estate (Regulation and Development) Act, 2016 .

- (g) any derivative transaction entered into in connection with protection against or benefit from fluctuation in any rate or price and for calculating the value of any derivative transaction, only the market value of such transaction shall be taken into account.
- (h) any counter-indemnity obligation in respect of a guarantee, indemnity, bond, documentary letter of credit or any other instrument issued by a bank or financial institution.
- (i) the amount of any liability in respect of any of the guarantee or indemnity for any of the items referred to in sub-clauses (a) to (h) of this clause [Section 5(8) of Code, 2016]

Subscription money for purchase of shares is not financial debt - Subscription money for purchase of shares is not financial debt - *ACPC Enterprises v. Affinity Beauty Saloon (2018)* (NCLT – Delhi Bench)

Operational debt as per section 5(21) of the Code means a claim in respect of the provision of goods or services including employment or a debt in respect of the payment of dues arising under any law for the time being in force and payable to the Central Government, any State Government or any local authority;

- (8) **Default** means non-payment of debt when whole or any part or instalment of the amount of debt has become due and payable and is not paid by the debtor or the corporate debtor, as the case may be. [Section 3(12)]
- (9) **Financial service** includes any of the following services, namely:—
 - (a) accepting of deposits;
 - (b) safeguarding and administering assets consisting of financial products, belonging to another person, or agreeing to do so;
 - (c) effecting contracts of insurance;

- (d) offering, managing or agreeing to manage assets consisting of financial products belonging to another person;
- (e) rendering or agreeing, for consideration, to render advice on or soliciting for the purposes of—
 - (i) buying, selling, or subscribing to, a financial product;
 - (ii) availing a financial service; or
 - (iii) exercising any right associated with a financial product or financial service;
- (f) establishing or operating an investment scheme;
- (g) maintaining or transferring records of ownership of a financial product;
- (h) underwriting the issuance or subscription of a financial product; or
- (i) selling, providing, or issuing stored value or payment instruments or providing payment services; [Section 3(16)]

- (10) **Financial Service Provider** means a person engaged in the business of providing financial services in terms of authorisation issued or registration granted by a financial sector regulator [Section 3(17)]

Financial Service Providers include banks, financial institutions, insurance companies, mutual funds etc.

- (11) **Financial Sector Regulator** means an authority or body constituted under any law for the time being in force to regulate services or transactions of financial sector and includes-

- the Reserve Bank of India,
- the Securities and Exchange Board of India,
- the Insurance Regulatory and Development Authority of India,
- the Pension Fund Regulatory Authority, and
- such other regulatory authorities as may be notified by the Central Government; [Section 3(18)]

- (12) **Insolvency professional (IP)** means a person enrolled under section 206 with an insolvency professional agency as its member and registered with the Board as an insolvency professional under section 207; [Section 3(19)]

Insolvency Professional is required to play a key role in implementation of the Code.

The word 'person', used refers to an individual to be IP. A LLP, partnership firm or a company can only be recognized as 'Insolvency Professional Entity' (IPE), which is not defined under the Code.

The Insolvency Professional should follow code of conduct as specified in section 208(2) of Insolvency Code and in First Schedule to Insolvency and Bankruptcy Board of India (Insolvency Professionals) Regulations, 2016.

- (13) **"Insolvency professional agency"** means any person registered with the Board under section 201 as an insolvency professional agency; [Section 3(20)]

Work relating to insolvency resolution is expected to be handled by 'Insolvency Professionals' (IP). These professionals are required to be registered with 'Insolvency Professional Agency' (IPA).

The Insolvency Professional Agencies (IPA) will develop professional standards, code of ethics and be first level regulator for insolvency professionals members. This will lead to development of a competitive industry for such professionals.

- (14) **"Information utility"** means a person who is registered with the Board as an information utility under section 210; [Section 3(21)]

The Insolvency and Bankruptcy processes are expected to function on basis of financial information available electronically.

Information Utility will collect, collate, authenticate and disseminate financial information to be used in insolvency, liquidation and bankruptcy proceedings.

- (15) A **person** includes:-

- an individual
- a Hindu Undivided Family
- a company
- a trust
- a partnership
- A limited liability partnership, and
- any other entity established under a Statute.

And includes a person resident outside India [Section 3(23)]

"Person resident outside India" means a person other than a person resident in India [section 3(25)].

"Person resident in India" shall have the meaning as assigned to such term in section 2(v) of FEMA [Section 3(24)]

- (16) **Property** includes money, goods, actionable claims, land and every description of property situated in India or outside India and every description of interest including present or future or vested or contingent interest arising out of, or incidental to, property; [Section 3(27)]

- (17) **Secured creditor** means a creditor in favour of whom security interest is created; [Section 3(30)]
- (18) **Security Interest** means right, title or interest or a claim to property, created in favour of, or provided for a secured creditor by a transaction which secures payment or performance of an obligation and includes mortgage, charge, hypothecation, assignment and encumbrance or any other agreement or arrangement securing payment or performance of any obligation of any person. [Section 3(31)]
- (19) A **transaction** includes an agreement or arrangement in writing for transfer of assets, or funds, goods or services, from or to the corporate debtor. [Section 3(33)]
- (20) **Transfer** includes sale, purchase, exchange, mortgage, pledge, gift, loan or any other form of transfer of right, title, possession or lien. [Section 3(34)]
- (21) **Adjudicating Authority-** National Company Law Tribunal (NCLT) constituted under section 408 of the Companies Act, 2013 is the Adjudicating Authority (AA) for purpose of insolvency resolution and liquidation for corporate persons and personal guarantors thereof [section 5(1) read with section 60(1) of the Code]

NCLT is also AA for the insolvency resolution or liquidation or bankruptcy of the corporate guarantor or personal guarantor of such CD when insolvency resolution or liquidation of such CD is pending before AA. [Section 60(2) of the Code]

National Company Law Appellate Tribunal (NCLAT) is the appellate authority over decisions of NCLT [section 61 of the Code]

Appeal against order of NCLAT can be filed to Supreme Court on question of law arising out of such order, within 45 days [section 62 of the Code]

Debt Recovery Tribunal (DRT) will be adjudicating authority for individuals and firms subject to section 60(2) – [section 179(1) of the Code]

- (22) **"Base resolution plan"** means a resolution plan provided by the corporate debtor under clause (c) of sub-section (4) of section 54A, which deals with the Corporate debtors eligible for pre-packaged insolvency resolution process; [Section 5(2A)]
- (23) **Corporate applicant means—**

- (a) corporate debtor; or
- (b) a member or partner of the corporate debtor who is authorised to make an application for the corporate insolvency resolution process or the pre-packaged insolvency resolution process, as the case may, under the constitutional document of the corporate debtor; or
- (c) an individual who is in charge of managing the operations and resources of the corporate debtor; or

- (d) a person who has the control and supervision over the financial affairs of the corporate debtor; [Section 5(5)]
- (24) **Corporate guarantor** means a corporate person who is the surety in a contract of guarantee to a corporate debtor; [Section 5(5A)]
- (25) **Dispute** includes a suit or arbitration proceedings relating to—
- (a) the existence of the amount of debt;
 - (b) the quality of goods or service; or
 - (c) the breach of a representation or warranty; [Section 5(6)]
- (26) **Financial creditor** means any person to whom a financial debt is owed and includes a person to whom such debt has been legally assigned or transferred to; [section 5(7)]
- (27) **Financial Debt** means a debt along with interest, if any, which is disbursed against the consideration for the time value of money and includes—
- (a) money borrowed against the payment of interest;
 - (b) any amount raised by acceptance under any acceptance credit facility or its dematerialised equivalent;
 - (c) any amount raised pursuant to any note purchase facility or the issue of bonds, notes, debentures, loan stock or any similar instrument;
 - (d) the amount of any liability in respect of any lease or hire purchase contract which is deemed as a finance or capital lease under the Indian Accounting Standards or such other accounting standards as may be prescribed;
 - (e) receivables sold or discounted other than any receivables sold on non-recourse basis;
 - (f) any amount raised under any other transaction, including any forward sale or purchase agreement, having the commercial effect of a borrowing;

Explanation -For the purposes of this sub-clause -

- (i) any amount raised from an allottee under a real estate project shall be deemed to be an amount having the commercial effect of a borrowing; and
 - (ii) the expressions, “allottee” and “real estate project” shall have the meanings respectively assigned to them in clauses (d) and (zn) of section 2 of the Real Estate (Regulation and Development) Act, 2016;
- (g) any derivative transaction entered into in connection with protection against or benefit from fluctuation in any rate or price and for calculating the value of any derivative transaction, only the market value of such transaction shall be taken into account;

- (h) any counter-indemnity obligation in respect of a guarantee, indemnity, bond, documentary letter of credit or any other instrument issued by a bank or financial institution;
- (i) the amount of any liability in respect of any of the guarantee or indemnity for any of the items referred to in sub-clause (a) to (h) of this clause; [Section 5(8)]
- (28) **Initiation date** means the date on which a financial creditor, corporate applicant or operational creditor, as the case may be, makes an application to the Adjudicating Authority for initiating corporate insolvency resolution process or pre-packaged insolvency resolution process, as the case may be; [Section 5(11)]
- (29) **Insolvency commencement date** means the date of admission of an application for initiating corporate insolvency resolution process by the Adjudicating Authority under sections 7, 9 or section 10, as the case may be; [Section 5(12)]
- (30) **Insolvency resolution process period** means the period of one hundred and eighty days beginning from the insolvency commencement date and ending on one hundred and eightieth day; [Section 5(14)]
- (31) **Liquidation commencement date** means the date on which proceedings for liquidation commence in accordance with section 33 (Initiation of Liquidation) or section 59 (Voluntary Liquidation of corporate persons), as the case may be; [Section 5(17)]
- (32) **Liquidator** means an insolvency professional appointed as a liquidator in accordance with the provisions of Chapter III or Chapter V of this Part, as the case may be;
- (33) **Operational creditor** means a person to whom an operational debt is owed and includes any person to whom such debt has been legally assigned or transferred; [Section 5(20)]
- (34) **Personal guarantor** means an individual who is the surety in a contract of guarantee to a corporate debtor; [Section 5(22)]
- (35) **Related party, in relation to a corporate debtor, means—**
 - (a) **a director or partner or a relative** of a director or partner of the corporate debtor
 - (b) **a key managerial personnel or a relative** of a key managerial personnel of the corporate debtor;
 - (c) **a limited liability partnership or a partnership firm** in which a director, partner, or manager of the corporate debtor or his relative is a partner;
 - (d) **a private company** in which a director, partner or manager of the corporate debtor is a director and holds along with his relatives, more than two per cent. of its share capital;
 - (e) **a public company** in which a director, partner or manager of the corporate debtor is a director and holds along with relatives, more than two per cent. of its paid-up share capital;

- (f) **any body corporate** whose board of directors, managing director or manager, in the ordinary course of business, acts on the advice, directions or instructions of a director, partner or manager of the corporate debtor;
 - (g) **any limited liability partnership or a partnership firm** whose partners or employees in the ordinary course of business, acts on the advice, directions or instructions of a director, partner or manager of the corporate debtor;
 - (h) **any person** on whose advice, directions or instructions, a director, partner or manager of the corporate debtor is accustomed to act;
 - (i) **a body corporate which is a holding, subsidiary or an associate company** of the corporate debtor, or a subsidiary of a holding company to which the corporate debtor is a subsidiary;
 - (j) **any person who controls** more than twenty per cent. of voting rights in the corporate debtor on account of ownership or a voting agreement;
 - (k) **any person in whom the corporate debtor controls** more than twenty per cent. of voting rights on account of ownership or a voting agreement;
 - (l) **any person who can control the composition** of the board of directors or corresponding governing body of the corporate debtor;
 - (m) **any person who is associated with the corporate debtor** on account of—
 - (i) participation in policy making processes of the corporate debtor; or
 - (ii) having more than two directors in common between the corporate debtor and such person; or
 - (iii) interchange of managerial personnel between the corporate debtor and such person;
 - (iv) provision of essential technical information to, or from, the corporate debtor; [Section 5(24)]
- (36) **"related party", in relation to an individual**, means—
- (a) a person who is a relative of the individual or a relative of the spouse of the individual;
 - (b) a partner of a limited liability partnership, or a limited liability partnership or a partnership firm, in which the individual is a partner;
 - (c) a person who is a trustee of a trust in which the beneficiary of the trust includes the individual, or the terms of the trust confers a power on the trustee which may be exercised for the benefit of the individual;

- (d) a private company in which the individual is a director and holds along with his relatives, more than two per cent of its share capital;
- (e) a public company in which the individual is a director and holds along with relatives, more than two per cent of its paid-up share capital;
- (f) a body corporate whose board of directors, managing director or manager, in the ordinary course of business, acts on the advice, directions or instructions of the individual;
- (g) a limited liability partnership or a partnership firm whose partners or employees in the ordinary course of business, act on the advice, directions or instructions of the individual;
- (h) a person on whose advice, directions or instructions, the individual is accustomed to act;
- (i) a company, where the individual or the individual along with its related party, own more than fifty per cent of the share capital of the company or controls the appointment of the board of directors of the company.

Explanation.—For the purposes of this clause,—

- (a) "relative", with reference to any person, means anyone who is related to another, in the following manner, namely:—
 - (i) members of a Hindu Undivided Family,
 - (ii) husband,
 - (iii) wife,
 - (iv) father,
 - (v) mother,
 - (vi) son,
 - (vii) daughter,
 - (viii) son's daughter and son,
 - (ix) daughter's daughter and son,
 - (x) grandson's daughter and son,
 - (xi) granddaughter's daughter and son,
 - (xii) brother,
 - (xiii) sister,
 - (xiv) brother's son and daughter,
 - (xv) sister's son and daughter,
 - (xvi) father's father and mother,
 - (xvii) mother's father and mother,

- (xviii) father's brother and sister,
- (xix) mother's brother and sister, and
- (b) wherever the relation is that of a son, daughter, sister or brother, their spouses shall also be included; [Section 5(24A)]
- (37) **"Resolution applicant"** means a person, who individually or jointly with any other person, submits a resolution plan to the resolution professional pursuant to the invitation made under section 25(2)(h) or pursuant to section 54K, as the case may be [Section 5(25)]
- (38) **"Resolution plan"** means a plan proposed by resolution applicant for insolvency resolution of the corporate debtor as a going concern in accordance with Part II; [Section 5(26)]
 Explanation.- For removal of doubts, it is hereby clarified that a resolution plan may include provisions for the restructuring of the corporate debtor, including by way of merger, amalgamation and demerger
- (39) **Resolution professional**, for the purposes of this Part, means an insolvency professional appointed to conduct the corporate insolvency resolution process or the pre-packaged insolvency resolution process, as the case may be, and includes an interim resolution professional; [Section 5(27)]
- (40) **Voting share** means the share of the voting rights of a single financial creditor in the committee of creditors which is based on the proportion of the financial debt owed to such financial creditor in relation to the financial debt owed by the corporate debtor. [Section 5(28)]



3. CORPORATE INSOLVENCY RESOLUTION PROCESS [SECTIONS 4, 6-32 AND 32A]

Provisions related to Insolvency Resolution and Liquidation process for Corporate Persons are covered in Part II of the Code. This part comprises of seven chapters with section 4 to 77 of the Code. Each chapter deals with different issues relating to Insolvency Resolution and Liquidation of Corporate Persons.

Corporate Insolvency Resolution Process (CIRP) is a process during which the Committee of Creditors (CoC) assess whether the debtor's business is feasible and viable to continue, the options for its rescue and revival, if any and endeavour is to keep it as a going concern. If the insolvency resolution process fails or CoC decide that the business of debtor cannot be revived then, the debtor will undergo liquidation process and the assets of the debtor shall be realized and distributed by the liquidator among the stakeholders as per Sec 53. The liquidation can also be on a going concern basis where the corporate debtor shall not be dissolved.

The Insolvency Resolution Process provides a collective mechanism to lenders to deal with the overall distressed position of a corporate debtor. This is a significant departure from the earlier legal

framework under which the primary onus to initiate a re-organization process lies with the debtor, and lenders may pursue distinct actions for recovery, security enforcement and debt restructuring.

The Code creates time-bound processes for insolvency resolution of companies and individuals. These processes is to be completed within 180 days, extendable by 90 days, however the overall process has to be completed within an outer time limit of 330 days. However, in certain exceptional cases, it may be open for the Adjudicating Authority and/or Appellate Tribunal to extend the time beyond 330 days³.

The Code also provides for fast-track resolution of corporate insolvency within 90 days. If insolvency cannot be resolved, the assets of the borrowers may be sold to repay creditors.

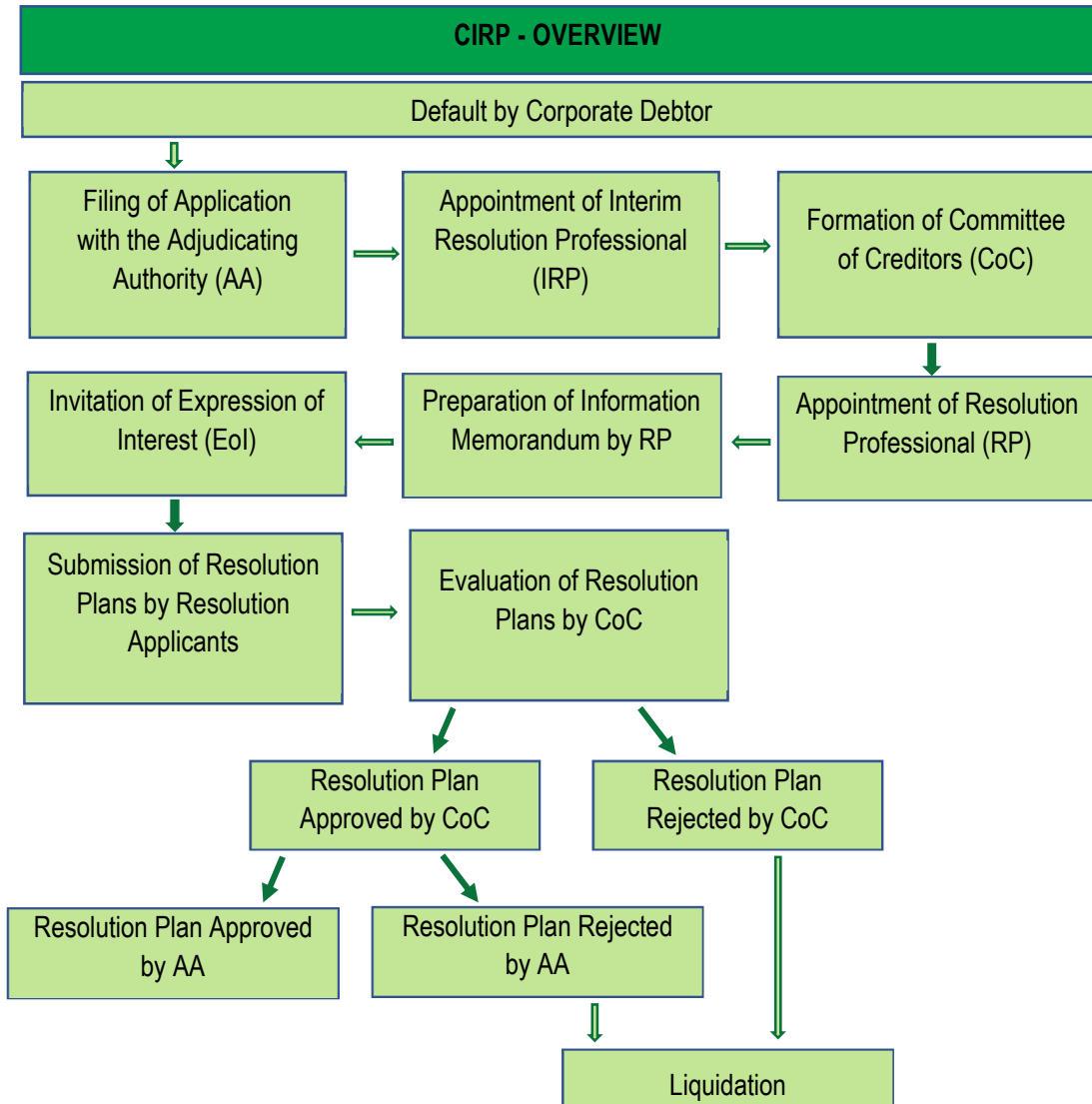
Process Flow

A comprehensive process that covers the gamut of insolvency resolution framework for Corporates and includes processes relating to:-

- Filing of application before NCLT by a financial creditor, operational creditor or a corporate applicant;
- Adjudication: Admission or Rejection of application. If admitted then:
 - Moratorium and Public Announcement;
 - Appointment of Interim Resolution Professional ;
 - Calling of claims ;
 - Formation of the Committee of Creditors
 - Appointment of Resolution Professional
 - Taking control and managing the operations of the corporate debtor by the IRP/ RP
 - Appointment of Registered Valuers
 - Preparation of Information memorandum & Invitation for Expression of Interest
 - Submission of Expression of Interest by prospective resolution applicants
 - Preparation of provisional and final list of resolution applicants by the Resolution Professional.
 - Issue of Request for Resolution Plan (RFRP), Information Memorandum and Evaluation Matrix to all the prospective resolution applicants
 - Submission of Resolution Plan by resolution applicants
 - Approval or rejection of the Resolution Plan by the CoC

³ CoC of Essar Steel India Limited vs. Satish Kumar Gupta & Ors. (Civil Appeal No. 8766-67 of 2019)

- Approval or rejection of the Resolution Plan by the NCLT (Adjudicating Authority)
- Implementation of Resolution Plan if approved by NCLT



(I) Application to National Company Law Tribunal

The process of insolvency is triggered by occurrence of default. As per Section 3 (12) of the Code, **default** means non-payment of debt when whole or any part or installment of the amount of debt has become due and payable and is not paid by the debtor or the corporate debtor.

The provisions relating to the insolvency and liquidation of corporate debtors shall be applicable only when the amount of the default is one lakh rupees or more. However, the Central Government has

by notification dated 24th March 2020 raised the threshold value of minimum amount of default to one crore rupees (section 4).

Provided further that the Central Government may, by notification, specify such minimum amount of default of higher value, which shall not be more than one crore rupees, for matters relating to the pre-packaged insolvency resolution process of corporate debtors under Chapter III-A.

Filing of application before NCLT

The corporate insolvency process may be initiated against any defaulting corporate debtor by making an application for corporate insolvency resolution process before NCLT.

(II) Who can initiate insolvency resolution process?

Where any corporate debtor commits a default, a financial creditor, an operational creditor or the corporate debtor itself may initiate corporate insolvency resolution process in respect of such corporate debtor in the manner as provided under this Chapter (Chapter II of part II) [Section 6].

Provisions and procedures relating to each initiator are different.

Accordingly, the application may be made by:-

Financial creditor any person to whom a financial debt is owed &

- Includes a person to whom such debt is legally assigned or transferred;

Operational creditor any person to whom a operational debt is owed &

- Includes a person to whom such debt is legally assigned or transferred ;

Corporate debtor A corporate person who owes a debt to any person and committed default.

(A) Initiation of corporate insolvency resolution process by financial creditor

- (1) **Filing of application before adjudicating authority:** A financial creditor either by itself or jointly with other financial creditors, or any other person on behalf of the financial creditor, as may be notified by the Central Government, may file an application for initiating corporate insolvency resolution process against a corporate debtor before the Adjudicating Authority when a default has occurred.

Provided that for the financial creditors, **referred to in clauses (a) and (b) of sub-section (6A) of section 21**, an application for initiating corporate insolvency resolution process against the corporate debtor **shall be filed jointly** by not less than one hundred of such creditors in the same class or not less than ten per cent, of the total number of such creditors in the same class, whichever is less:

Provided further that for **financial creditors who are allottees** under a real estate project, an application for initiating corporate insolvency resolution process against the corporate

debtor **shall be filed jointly** by not less than one hundred of such allottees under the same real estate project or not less than ten per cent, of the total number of such allottees under the same real estate project, whichever is less:

Explanation: For the purposes of this sub-section, a default includes a default in respect of a financial debt owed not only to the applicant financial creditor but to any other financial creditor of the corporate debtor.

Vide Notification S.O.1091(E) dated 27th February, 2019, the Central government hereby notified following persons who may file an application for initiating corporate insolvency resolution process against a corporate debtor before the Adjudicating Authority, on behalf of the Financial Creditor:-

- (i) a guardian;
 - (ii) an executor or administrator of an estate of a financial creditor;
 - (iii) a trustee (including a debenture trustee); and
 - (iv) a person duly authorized by the Board of Directors of a Company.
- (2) **Procedure to be followed by the Financial creditor:** The financial creditor shall file an application by itself / jointly against a corporate debtor before NCLT in accordance with the provisions contained in Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016, Copy of such an application shall be forwarded to registered office of corporate debtor and to the Board, by registered post or speed post or by hand or by electronic means, before filing with the Adjudicating Authority .

Financial creditor shall along with the application furnish—

- (a) **record of the default** recorded with the information utility or such other record or evidence of default as may be specified;
 - (b) **the name of the insolvency professional** proposed to act as an interim resolution professional; and
 - (c) **any other information** as may be specified by the Board.
- (3) **Time period for determination of default:** The Adjudicating Authority shall, within fourteen days of the receipt of the application, ascertain the existence of a default from the records of an information utility or on the basis of other evidence furnished by the financial creditor.

Provided that if the Adjudicating Authority has not ascertained the existence of default and passed an order within such time as specified, it shall record its reasons in writing for the same.

Case Law

Supreme Court in *Surendra Trading Company Vs. Juggilal Kamlatpat Jute Mills Company Ltd. & Others* prescribed time period for determination of defaults. It was held that the time limit prescribed in IBC, 2016 for admitting or rejecting a petition or initiation of CIRP under proviso to sub-section (5) of section 7 or sub-section (5) of section 9 or sub-section (4) of section 10 is procedural in nature, a tool of aid in expeditious dispensation of justice and is directory.

Various provisions of the Code would indicate that there are three stages:

(i) First stage: Filing of the application: When the application is filed, the Registry of the Adjudicating Authority is supposed to scrutinize the same to find out as to whether it is complete in all respects or there are certain defects. If it is complete, the same shall be posted for preliminary hearing before the Adjudicating Authority.

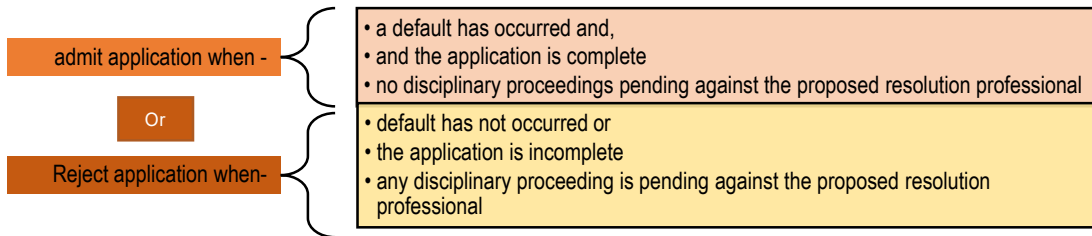
If there are defects, the applicant would be notified about those defects so that these are removed. For this purpose, seven days' time is given. Once the defects are removed then the application would be posted before the Adjudicating Authority.

(ii) Second Stage: When the application is listed before the Adjudicating Authority: It has to take a decision to either admit or reject the application. For this purpose, fourteen days' time is granted to the Adjudicating Authority. If the application is rejected, the matter is given a quietus (i.e. dead) at that level itself. However, if it is admitted, we enter the third stage.

(iii) Third Stage: After admission of the application: As application is admitted, insolvency resolution process commences. This resolution process is to be completed within 180 days, which is extendable, in certain cases, up to 90 days. Insofar as the first stage is concerned, it has no bearing on the insolvency resolution process at all, inasmuch as, unless the application is complete in every respect, the Adjudicating Authority is not supposed to deal with the same. It is at the second stage that the Adjudicating Authority is to apply its mind and decide as to whether the application should be admitted or rejected. Here adjudication process starts. However, in spite thereof, when this period of fourteen days given by the statute to the Adjudicating Authority to take a decision to admit or reject the application is directory, there is no reason to make it mandatory in respect of the first stage, which is pre-adjudication stage.

Thus, provision of removing the defects within seven days is directory and not mandatory in nature.

- (4) **Order:** Where the Adjudicating Authority is satisfied, it may either —



Notice to rectify the defect in the application: Provided that the Adjudicating Authority shall, before rejecting the application, give a notice to the applicant to rectify the defect in his application **within seven days** of receipt of such notice from the Adjudicating Authority. It is applicable for all kind of applications filed i.e. by Financial Creditor or Operational Creditor or by the Corporate Debtor.

- (5) **Commencement of corporate insolvency resolution process:** The corporate insolvency resolution process shall commence from the date of admission of the application.

- (6) **Communication of Order:** The Adjudicating Authority shall communicate order of admission or rejection of such application within seven days, as the case may be —

- (1) in case of admission, to the financial creditor and the corporate debtor;
- (2) In case of rejection, to the financial creditor [Section 7]

- (7) **Withdrawal of application:** Withdrawal of application shall be pursuant to Section 12A of the Code read with Regulation 30A of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016. The following scenarios may arise for withdrawal of application:

1. Before admission of application

An application initiating CIRP may be withdrawn before its admission, at any time with the permission of the Adjudicating Authority. [Rule 8 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016]

2. After admission of application

Once application is admitted, further three scenarios may arise:

(a) Before Constitution of CoC

- The applicant shall make an application for withdrawal to the Adjudicating Authority through the interim resolution professional;

(b) After Constitution of CoC but before issue of Invitation for Expression of Interest ("EoI")

- An application for withdrawal shall be firstly considered by the CoC, within seven days of its receipt.
- Such withdrawal application shall be approved by the CoC with ninety percent voting share,
- upon which the resolution professional shall submit such withdrawal application along with the approval of the committee,
- to the Adjudicating Authority on behalf of the applicant,
- within three days of such approval.

(c) After issue of invitation for EoI

- The same procedure as stipulated for scenario 'b' above shall apply.
- However, in this scenario, the applicant shall state the reasons justifying withdrawal after issue of such invitation.

In all the above scenarios, the final approval of such withdrawal shall be by way of an order passed by the Adjudicating Authority.

Case Laws

1. National Company Law Tribunal, Mumbai Bench in *Bank of India v. Future Retail Ltd.* in 2022, came with an issue, where a financial creditor had provided various credit facilities and non-fund-based limits to corporate debtor. It were restructured under a sanctioned letter and framework agreement. Corporate debtor defaulted in repayment and account of corporate debtor was classified as a non-performing asset (NPA). Meanwhile, corporate debtor issued a letter to financial creditor and certain other lenders for one-time restructuring (OTR) facilities under 'resolution frame work agreement for Covid 19 related stress as per RBI Circular. Financial creditor considered corporate debtor's request allowing OTR and executed a framework agreement for restructuring of existing outstanding amount. However, corporate debtor again defaulted in repayment of an outstanding amount. Financial creditor filed petition under section 7. It was noted that corporate debtor, on payment obligation under OTR scheme, admitted default of its repayment and further, corporate debtor admitted outstanding amount in its meeting with lenders that events of default continued to subsist. It was held, in view of facts, that existence of debt and default had been proved and, therefore, petition filed by financial creditor to initiate CIRP against corporate debtor was admitted.

2. National Company Law Appellate Tribunal, New Delhi, in 2022 in *Siti Networks Ltd. v. Assets Care and Reconstruction Enterprises Ltd.* decided on continuation of proceeding by assignee on an application seeking substitution as financial creditor in place of original financial creditor.

In the given case, financial creditor sanctioned a loan to corporate debtor, however, corporate debtor failed and was classified as non-performing asset. Financial creditor filed an application under section 7 against corporate debtor and same was admitted by NCLT. Later, financial creditor vide registered assignment deed, assigned debt of corporate debtor to respondent i.e. assignee. Corporate debtor was informed about aforesaid assignment. Subsequently, assignee filed an application seeking substitution as financial creditor in place of original financial creditor and was permitted by NCLT to pursue application filed by original financial creditor. Challenging said order, instant appeal was filed by corporate debtor. It was held that section 5(7) of the Code defines financial creditor, also includes a person to whom such debt has been legally assigned or transferred to. Therefore by virtue of assignment, assignee became financial creditor and had stepped in shoes of original financial creditor and assignee had every right to continue proceeding, which was initiated by original financial creditor.

3. SC in *Manish Kumar v. Union of India* in 2021 came up with a decision on section 7 by section 3 of IBC (Amendment) Act, 2020 requiring minimum threshold for initiation of proceedings (class action) by certain categories of financial creditors against corporate debtors such as real estate developers, are Constitutionally Valid.

In the given case, CIRP was initiated by the Financial creditors requiring minimum threshold for initiation of proceedings (class action) by certain categories of financial creditors against corporate debtors such as real estate developers.

According to Provisos of section 7, it was required that in case of a real estate project, being conducted by a corporate debtor, an application can be filed by either one hundred allottees or allottees constituting one-tenth of allottees, whichever is less, if they are able to establish a default in regard to a financial creditor and it is not necessary that there must be default *qua* any of Applicants. It was held that since default can be *qua* any of applicants and even a person who is not an applicant and action is one which is understood to be in rem, in that, procedures under Code would bind entire set of stakeholders including whole of allottees.

(B) Initiation of corporate insolvency resolution process by operational creditor

- (1) Serving of demand Notice:** On the occurrence of default, an operational creditor shall first send a demand notice and a copy of invoice to the corporate debtor in such form and manner as may be ⁴prescribed.

"Demand notice" means a notice served by an operational creditor to the corporate debtor demanding payment of the operational debt in respect of which the default has occurred.

On receipt of demand notice by corporate debtor: The corporate debtor shall, within a period of ten days of the receipt of the demand notice or copy of the invoice, bring to the notice of the operational creditor about-

- (a) **existence of a dispute about debt**, if any, record of the pendency of the suit or arbitration proceedings filed before the receipt of such notice or invoice in relation to such dispute;
- (b) **the payment of unpaid operational debt**— It is possible that corporate debtor might have already paid the unpaid operational debt, there in such situation, corporate debtor will inform within 10 days -
 - (i) by sending an attested copy of the record of electronic transfer of the unpaid amount from the bank account of the corporate debtor; or
 - (ii) by sending an attested copy of record that the operational creditor has encashed a cheque issued by the corporate debtor. [Section 8]

(2) Application for initiation of Corporate Insolvency Resolution Process by operational creditor after issue of demand notice:

- (i) **Filing of application by operational creditor:** If no reply is received or payment or notice of the dispute under section 8(2) from the corporate debtor within ten days from the date of delivery of the notice or invoice demanding payment, or even if reply is received disputing the claim and operations creditors feels that the dispute is vague or untenable, operational creditor can file application⁵ before Adjudicating Authority (NCLT) for initiating a corporate insolvency resolution process.
- (ii) **Providing of documents/ information:** The operational creditor shall, along with the application filed in prescribed form, furnish the following documents—

⁴ Rule 5, Form 3 & Form 4 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016.

⁵ Rules 6, 8, 9 & 10 and Form 5 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016

a copy of the invoice , or demand notice

- demanding payment, or delivered by the operational creditor to the corporate debtor;

an affidavit

- to the effect that there is no notice given by the corporate debtor relating to a dispute of the unpaid operational debt

a copy of the certificate

- from the financial institutions maintaining accounts of the operational creditor confirming that there is no payment of an unpaid operational debt by the corporate debtor, if available;

a copy of a record with information utility

- confirming that there is no payment of an unpaid operational debt by the corporate debtor, if available; and

any other proof

- confirming that there is no payment of an unpaid operational debt by the corporate debtor, or

such other information,

- as may be prescribed.

- (3) **Appointment of IRP:** An operational creditor initiating a corporate insolvency resolution process, may propose a insolvency professional to act as an interim resolution professional.
- (4) **Order of an adjudicating authority:** The Adjudicating Authority shall, within fourteen days of the receipt of the application, by an order—

admit the application and communicate such decision to the operational creditor and the corporate debtor if,—	reject the application and communicate such decision to the operational creditor and the corporate debtor, if—
(a) the application made is complete; (b) there is no payment of the unpaid operational debt; (c) the invoice or notice for payment to the corporate debtor has been delivered by the operational creditor; (d) no notice of dispute has been received by the operational creditor or there is no record of dispute in the information utility; and (e) there is no disciplinary proceeding pending against any resolution professional proposed, if any.	(a) the application made is incomplete; (b) there has been payment of the unpaid operational debt; (c) the creditor has not delivered the invoice or notice for payment to the corporate debtor; (d) notice of dispute has been received by the operational creditor or there is a record of dispute in the information utility; or (e) any disciplinary proceeding is pending against any proposed resolution professional: Provided that Adjudicating Authority, shall before rejecting an application which is incomplete, give a notice to the applicant to rectify the defect in his application within seven days of the date of receipt of such notice from the adjudicating Authority.

- (5) **Withdrawal of application before or after admission:** The same procedure as stated under initiation of CIRP by financial creditor shall apply here as well for withdrawal of application.
- (6) **Commencement of insolvency resolution process:** The corporate insolvency resolution process shall commence from the date of admission of the application [Section 9]

Case Laws

1. SC in the matter of *Mobilox Innovations Pvt. Ltd. Vs. Kirusa Software Pvt. Ltd.* Civil Appeal No. 9405 of 2017 dt 21st Sept 2017. It was decided that in sec 9 application if there is dispute then it cannot be admitted. It should not feeble legal argument or an assertion of facts unsupported by evidence and it need not be spurious, mere bluster, plainly frivolous or vexatious.
2. National Company Law Appellate Tribunal, Chennai in *Fipola Retail (India) (P.) Ltd. v. M2N Interiors* in 2021 admitted application filed by operational creditor under section 9 against corporate debtor in name of proprietary concern. Corporate debtor alleged that said application would not be maintainable as application had been filed in name of proprietary concern which is not a 'person' for purpose of filing application under section 9. It was held that such an application was maintainable, as section 2(f) provides that provisions of Code shall apply to partnership firms and proprietorship firm also.

(C) Initiation of corporate insolvency resolution process by corporate applicant.

- (1) **Commission of default:** Where a corporate debtor has committed a default, a **corporate applicant** thereof may file an application for initiating corporate insolvency resolution process with the Adjudicating Authority. The application shall be filed in such form, containing such particulars and in such manner and accompanied with such fee as may be prescribed.⁶

"Corporate applicant means – (a) Corporate debtor, or (b) a member or partner of the corporate debtor who is authorised to make an application for the corporate insolvency resolution process under the **constitutional document** of the corporate debtor; or (c) an individual who is in charge of managing the operations and resources of the corporate debtor; or (d) a person who has the control and supervision over the financial affairs of the corporate debtor;

"constitutional document", in relation to a corporate person, includes articles of association, memorandum of association of a company and incorporation document of a Limited Liability Partnership;

- (2) **Furnishing of information:** The corporate applicant shall, along with the application furnish the information relating to—

⁶ Rules 7, 8, 9 & 10 & Form 6 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016

- (a) its **books of account and such other documents** relating to such period as may be specified; and
 - (b) the **insolvency professional** proposed to be appointed as an interim resolution professional.
 - (c) **special resolution** passed by shareholders of the corporate debtor or the resolution passed by at least three-fourth of the total number of partners of the corporate debtor, as the case may be, approving filing of the application.
- (3) **Admission/rejection of application:** The Adjudicating Authority shall, within a period of fourteen days of the receipt of the application, by an order—
- (a) admit the application, if it is complete; and no disciplinary proceeding is pending against the proposed resolution professional
 - (b) reject the application, if it is incomplete or any disciplinary proceeding is pending against the proposed resolution professional

Provided that Adjudicating Authority shall, before rejecting an application, give a notice to the applicant to rectify the defects in his application within seven days from the date of receipt of such notice from the Adjudicating Authority.

Case Law

NCLT Mumbai Bench in CP (IB) 918/MB/C-II/2020 dt. 10th Oct 2020 in the matter of *IGOPL Offshore P Ltd* has pronounced that section 10(3)(c) of the Code requires that a Special Resolution passed by the shareholders of the Corporate Debtor needs to be filed along with the Company Petition.

- (4) **Commencement of insolvency resolution process:** The corporate insolvency resolution process shall commence from the date of admission of the application. [Section 10]

(III) Suspension of initiation of corporate insolvency resolution process

Notwithstanding anything contained in sections 7, 9 and 10, no application for initiation of corporate insolvency resolution process of a corporate debtor shall be filed, for any default arising on or after 25th March, 2020 for a period of six months or such further period, not exceeding one year from such date, as may be notified in this behalf:

Provided that no application shall ever be filed for initiation of corporate insolvency resolution process of a corporate debtor for the said default occurring during the said period.

Explanation- For the removal of doubts, it is hereby clarified that the provisions of this section shall not apply to any default committed under the said sections before 25th March, 2020. [Section 10A]

The provisions of section 10A was extended twice and it was applicable for default up to 25/3/2021.

(IV) Persons not entitled to initiate insolvency process

Following persons shall not be entitled to initiate the corporate insolvency process:-

- (a) A corporate debtor undergoing an insolvency resolution process or a pre-packaged insolvency resolution process; or
- (aa) A financial creditor or an operational creditor of a corporate debtor undergoing a pre-packaged insolvency resolution process; or
- (b) A corporate debtor having completed corporate insolvency resolution process 12 (twelve) months preceding the date of making of the application; or
- (ba) a corporate debtor in respect of whom a resolution plan has been approved under Chapter III-A, twelve months preceding the date of making of the application; or
- (c) A corporate debtor or a financial creditor who has violated any of the terms of resolution plan which was approved 12 (twelve) months before the date of making of an application;
- (d) A corporate debtor in respect of whom a liquidation order has been made.

Explanation 1 - For the purposes of this section, a corporate debtor includes a corporate applicant in respect of such corporate debtor.

Explanation 2- For the purposes of this section, it is hereby clarified that nothing in this section shall prevent a corporate debtor referred to in clauses (a) to (d) from initiating corporate insolvency resolution process against another corporate debtor. [Section 11]

Following categories of Corporate debtors not entitled to file an application under section 11

- Corporate debtor undergoing CIRP/PPIRP
- A financial creditor / operational creditor undergoing a PPIRP
- Corporate debtor having completed CIRP 12 months before the date of making of the application
- a corporate debtor in respect of whom a resolution plan has been approved under Chapter III-A, 12 months preceding the date of making of the application
- Corporate debtor violating the term of resolution plan
- Corporate debtor in respect of whom a liquidation order has been made

Example: Suppose ABC LLP ("Corporate Debtor") has committed a default. Mr. X and Mr. Y, are partners of the Corporate Debtor contributing to the capital and sharing profits/losses in the ratio of 49% and 51% respectively. However, Mr. Y under the constitutional document of the Company, is being authorized to make an application for the corporate insolvency resolution process. Being a partner of the Corporate Debtor, Mr. Y filed an application on behalf of the Corporate Debtor for initiation of corporate insolvency resolution process.

As per section 10 of the Code, initiation of CIRP by a Corporate Debtor shall be made by filing an application along with information relating to books of accounts, interim resolution professional and resolution passed by at least three-fourths of total number of partners. In the given case, even though Mr. Y is authorized to file an application for initiation of CIRP, such act shall not stand valid if the resolution authorizing such filing has not been passed by at least three-fourths of total number of partners.

(V) Disposal of applications under section 54C and under section 7 or section 9 or section 10

- (1) Where an application filed under section 54C is pending, the Adjudicating Authority shall pass an order to admit or reject such application under section 54C, before considering any application filed under section 7 or section 9 or section 10, in respect of the same corporate debtor.
- (2) Where an application under section 54C is filed within fourteen days of filing of any application under section 7 or section 9 or section 10, which is pending, in respect of the same corporate debtor, then, notwithstanding anything contained in sections 7, 9 or 10, the Adjudicating Authority shall first dispose of the application under section 54C.
- (3) Where an application under section 54C is filed after fourteen days of the filing of any application under section 7 or section 9 or section 10, in respect of the same corporate debtor, the Adjudicating Authority shall first dispose of the application under sections 7, 9 or 10.
- (4) The provisions of this section shall not apply where an application under section 7 or section 9 or section 10 is filed and pending as on the date of the commencement of the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2021. [Section 11A]

(VI) Adjudication: Admission or Rejection of Application

The Adjudicating Authority may either accept or reject the application within fourteen days of receipt of application. However, applicant should be allowed to rectify the defect within seven days of receipt of notice of such rejection.

The insolvency resolution process shall commence from the date of admission of application by the Adjudicating Authority. It is referred to as the Insolvency Commencement Date.

(VII) Time-limit for completion of insolvency resolution process

- (1) **Period for completion of insolvency process:** The corporate insolvency resolution process shall be completed within a period of **one hundred and eighty days** from the date of admission of the application to initiate such process.
- (2) **Filing of application for extension of period:** The resolution professional shall file an ⁷application to the Adjudicating Authority to extend the period of the corporate insolvency resolution process beyond one hundred and eighty days, if instructed to do so by a resolution

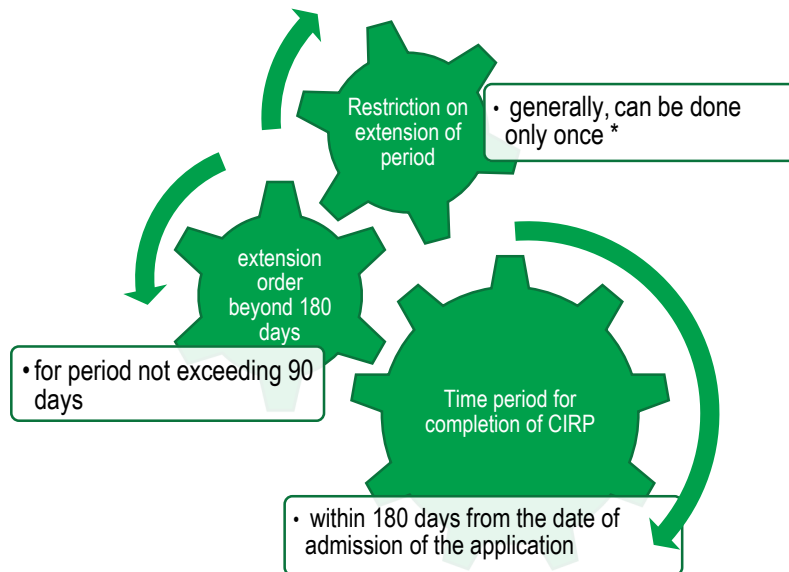
⁷ Under Regulation 40 of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016

passed at a meeting of the committee of creditors by a vote of sixty- six per cent (minimum) of the voting shares.

- (3) **Period of extension:** On receipt of an application, if the Adjudicating Authority is satisfied that the subject matter of the case is such that corporate insolvency resolution process cannot be completed within one hundred and eighty days, it may by order extend the duration of such process beyond one hundred and eighty days by such further period as it thinks fit, **but not exceeding ninety days:** Provided that any extension of the period of corporate insolvency resolution process under this section shall not be granted more than once.

Provided further that the corporate insolvency resolution process shall mandatorily be completed within a period of **three hundred and thirty days** from the insolvency commencement date, including any extension of the period of corporate insolvency resolution process granted under this section and the time taken in legal proceedings in relation to such resolution process of the corporate debtor:

Provided also that where the insolvency resolution process of a corporate debtor is pending and has not been completed within the period referred to in the second proviso, such resolution process shall be completed within a period of ninety days from the date of commencement of the Insolvency and Bankruptcy Code (Amendment) Act, 2019.



* Adjudicating Authority (NCLT) has power to extend the CIRP period beyond 270 days on the basis of reasonable justifications, in the interest of furtherance of the objectives of the Code.

(VIII) Appointment of Interim Resolution Professional

"Resolution Professional", means an insolvency professional appointed to conduct the corporate insolvency resolution process and includes an interim resolution professional.

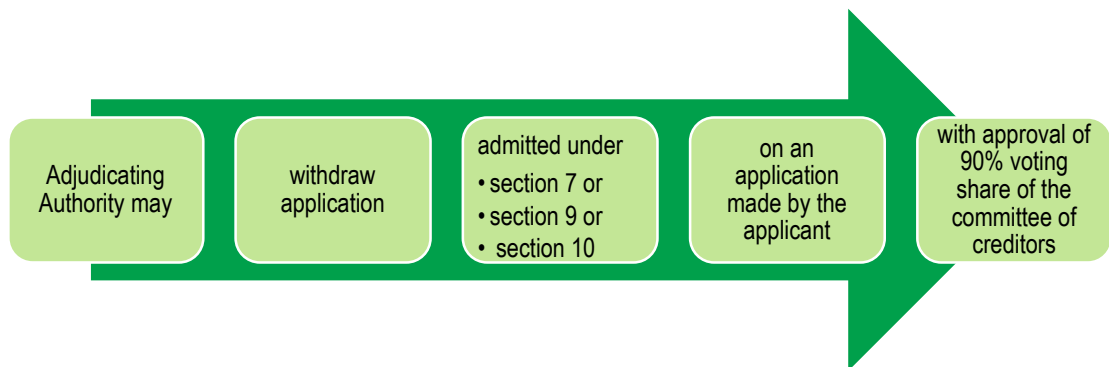
If applicant proposes for appointment of Insolvency professional

- obtain written communication from insolvency professional for appointment as interim resolution professional

(IX) Withdrawal of application admitted under section 7, 9 or 10 [Section 12A]

(1) **Before formation of Committee of Creditors:** Application can be withdrawn if settlement is there with the creditor and appropriate form is filed through IRP.

(2) **After Committee of Creditors is formed:**

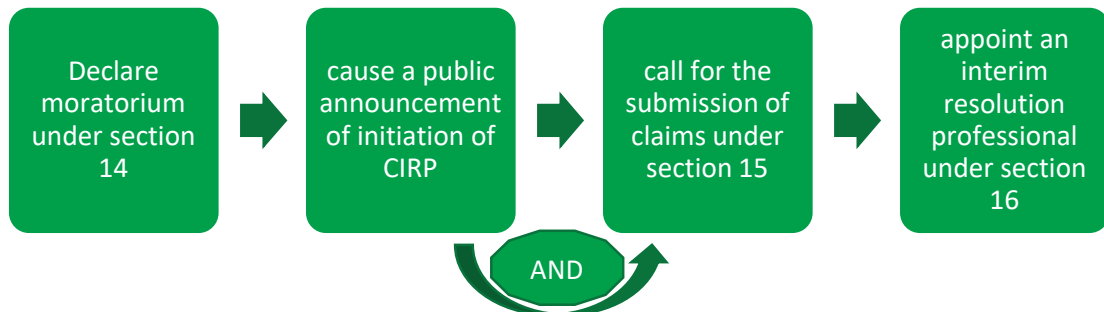


Case Law

SC in *Ashok G. Rajani v. Beacon Trusteeship Ltd.* said that Section 12A enables the NCLT to allow the withdrawal of an application admitted under section 7 or section 9 or section 10, on an application made by the applicant with the approval of 90 per cent voting shares of the Committee of Creditors. Section 12A clearly permits withdrawal of an application under section 7 that has been admitted on an application made by the applicant. The question of approval of the Committee of Creditors by the requisite percentage of votes, can only arise after the Committee of Creditors is constituted. Before the Committee of Creditors is constituted, there is, no bar to withdrawal by the applicant of an application admitted under section 7.

(X) Declaration of moratorium and public announcement:

After admission of application, the Adjudicating Authority shall pass following order —



The public announcement as referred above, shall be made immediately after the appointment of the interim resolution professional. **[Section 13]**

Moratorium:

Moratorium is a delay or suspension of an activity. In a legal context, it may refer to the temporary suspension of a law to allow a legal challenge to be carried out.

After the commencement of corporate insolvency resolution process a calm period, known as moratorium period is declared, during which all suits and legal proceedings etc. against the Corporate Debtor are held in abeyance to allow the IRP/ RP to carry out his/her task smoothly and disallowing creditors and other stakeholders to take any individual actions against the corporate debtor and disrupt the process.

- (1) **Declaration of moratorium period:** According to the section 14(1) of the Code, on the insolvency commencement date, the Adjudicating Authority shall by order, declare moratorium prohibiting all of the following, acts—
 - (a) **the institution of suits or continuation of pending suits or proceedings** against the corporate debtor including execution of any judgment, decree or order in any court of law, tribunal, arbitration panel or other authority;
 - (b) **transferring, encumbering, alienating or disposing of** by the corporate debtor any of its assets or any legal right or beneficial interest therein;
 - (c) **any action to foreclose, recover or enforce any security interest** created by the corporate debtor in respect of its property including any action under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;
 - (d) **the recovery of any property** by an owner or lessor where such property is occupied by or in the possession of the corporate debtor.

Explanation—For the purposes of this sub-section, it is hereby clarified that notwithstanding anything contained in any other law for the time being in force, a licence, permit, registration, quota, concession, clearance or a similar grant or right given by the Central Government, State Government, local authority, sectoral regulator or any other authority constituted under any other law for the time being in force, shall not be suspended or terminated on the grounds of insolvency, subject to the condition that there is no default in payment of current dues arising for the use or continuation of the license or a similar grant or right during moratorium period

- (2) **The supply of essential goods or services⁸** to the corporate debtor as may be specified shall not be terminated or suspended or interrupted during moratorium period.

⁸ Regulation 32 of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016

- (2A) Where the interim resolution professional or resolution professional, as the case may be, considers the supply of goods or services critical to protect and preserve the value of the corporate debtor and manage the operations of such corporate debtor as a going concern, then the supply of such goods or services shall not be terminated, suspended or interrupted during the period of moratorium, except where such corporate debtor has not paid dues arising from such supply during the moratorium period or in such circumstances as may be specified
- (3) **Prohibited Acts:** Acts prohibited during Moratorium period, shall not apply to-
- (a) Such transactions as may be notified by the Central Government in consultation with any financial sector regulator.
 - (b) A surety in a contract of guarantee to a corporate debtor.
- (4) **Effect of the order of moratorium:** The order of moratorium shall have effect from the date of such order till the completion of the corporate insolvency resolution process:

The provision of section 14(1) of the Code is not applicable on a surety in a contract of guarantee to a corporate debtor. Thus, recovery proceedings, insolvency resolution process or bankruptcy proceedings against surety (guarantor) can be initiated even if moratorium is granted to corporate debtor.

It is clarified that notwithstanding anything contained in any other law for the time being in force, a licence, permit, registration, quota, concession, clearance or a similar grant or right given by the Central Government, State Government, local authority, sectoral regulator or any other authority constituted under any other law for the time being in force, shall not be suspended or terminated on the grounds of insolvency, subject to the condition that there is no default in payment of current dues arising for the use or continuation of the license or a similar grant or right during moratorium period.

When Moratorium period shall cease to have effect

Provided that where at any time during the corporate insolvency resolution process period, if the Adjudicating Authority approves the resolution plan or passes an order for liquidation of corporate debtor, the moratorium shall cease to have effect from the date of such approval or liquidation order, as the case may be [Section 14]

Example: After commencement of Corporate Insolvency Resolution Process, NCLT declared Moratorium against the corporate debtor. Within a month of declaration, corporate debtor disposed of his property. In line with section 14 of the Code, any transaction/disposal of any assets of Corporate Debtor during the moratorium period, is prohibited. Such an act of the Corporate Debtor is not valid.

However, as per Regulation 29 of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016, the Resolution Professional may sell unencumbered asset(s) of the corporate debtor, other than in the ordinary course of business, not exceeding 10% of the total claims admitted.

Public Announcement

Interim Resolution Professional shall make the Public Announcement immediately after his appointment. "Immediately" refers to not more than **three days** from the date of appointment of the Interim Resolution Professional.

Particulars of the Public announcement: As per **Section 15** of the Code, public announcement shall include the followings and it shall be in the form prescribed :-

- a) Name & Address of Corporate Debtor under the Corporate Insolvency Resolution Process.
- b) Name of the authority with which the corporate debtor is incorporated or registered.
- c) Details of interim resolution Professional who shall be vested with the management of the Corporate Debtor and be responsible for receiving claims.
- d) Penalties for false or misleading Claims.
- e) The last date for the submission of the claims as may be specified.
- f) The date on which the Corporate Insolvency Resolution Process ends.

The expenses of public announcement shall be borne by the applicant or which may be reimbursed by the Committee of Creditors, to the extent it ratifies them.

(XI) Appointment, Term and Powers of Interim Resolution Professional (IRP)

Appointment of IRP: Adjudicating authority shall appoint an Interim Resolution Professional on the insolvency commencement date. Section 16 of the Code lays down the procedure for appointment of an Interim Resolution Professional.

Where the application for corporate insolvency resolution process is made by a financial creditor or the corporate debtor, the resolution professional as proposed in the application shall be appointed as the interim resolution professional, if no disciplinary proceedings are pending against him.

Where the **application for corporate insolvency resolution process is made by an operational creditor** and

- (a) **No name of an interim resolution professional is made.** The Adjudicating Authority shall make a reference to the Board for the recommendation of an insolvency professional who may be appointed to act as an interim resolution professional.
- (b) **A name of an interim resolution professional is made** the proposed resolution professional shall be appointed as the interim resolution professional, if no disciplinary proceedings are pending against him.

The Board shall recommend the name of an insolvency professional to the Adjudicating Authority against whom no disciplinary proceedings are pending, within ten days of the receipt of a reference from the Adjudicating Authority.

Period of appointment of IRP: The term of Interim Resolution Professional shall continue till the date of appointment of the resolution professional under section 22. **[Section 16]**

The key duties to be performed by the Interim Resolution Professional are:-

- (a) collect all information relating to the **assets, finances and operations of the corporate debtor** for determining the financial position of the corporate debtor
- (b) **Collation of claims** received pursuant to public announcement made
- (c) **Constitution of the Committee of Creditors**
- (d) **monitor the assets** of the corporate debtor **and manage its operations** until a resolution professional is appointed by the committee of creditors
- (e) **File information** collected with the information utility, if necessary
- (f) Take **control and custody of any assets** over which corporate debtor has ownership rights
- (g) **Perform other duties** as specified by the Board **[Section 18]**

Powers of IRP: As per section 17 of the Code, from the date of appointment of the interim resolution professional, the management of the affairs of the corporate debtor shall vest in the IRP—

- (a) The management of the affairs of the corporate debtor shall vest in the interim resolution professional. IRP shall be authorized to do the following:
 - act and execute in the name and on behalf of the corporate debtor all deeds, receipts, and other documents, if any;
 - take such actions, in the manner and subject to such restrictions, as may be specified by the Board;
 - have the authority to access the electronic records of corporate debtor from information utility having financial information of the corporate debtor;
 - have the authority to access the books of account, records and other relevant documents of corporate debtor available with government authorities, statutory auditors, accountants and such other persons as may be specified; and
 - be responsible for complying with the requirements under any law for the time being in force on behalf of the corporate debtor.
- (b) **Exercise of Power of BoD/ partners:** The powers of the board of directors or the partners of the corporate debtor, as the case may be, shall stand suspended and be exercised by the interim resolution professional.
- (c) **Reporting of officers/managers:** The officers and managers of the corporate debtor shall report to the interim resolution professional and provide access to such documents and records of the corporate debtor as may be required by the interim resolution professional.

- (d) **Instructions to financial institutions:** The financial institutions maintaining accounts of the corporate debtor shall act on the instructions of the interim resolution professional in relation to such accounts and furnish all information relating to the corporate debtor available with them to the interim resolution professional.

Management of operations of corporate debtor as going concern: The IRP shall make every endeavor to protect and preserve the value of the property of the corporate debtor and manage the operations of the corporate debtor as a going concern.

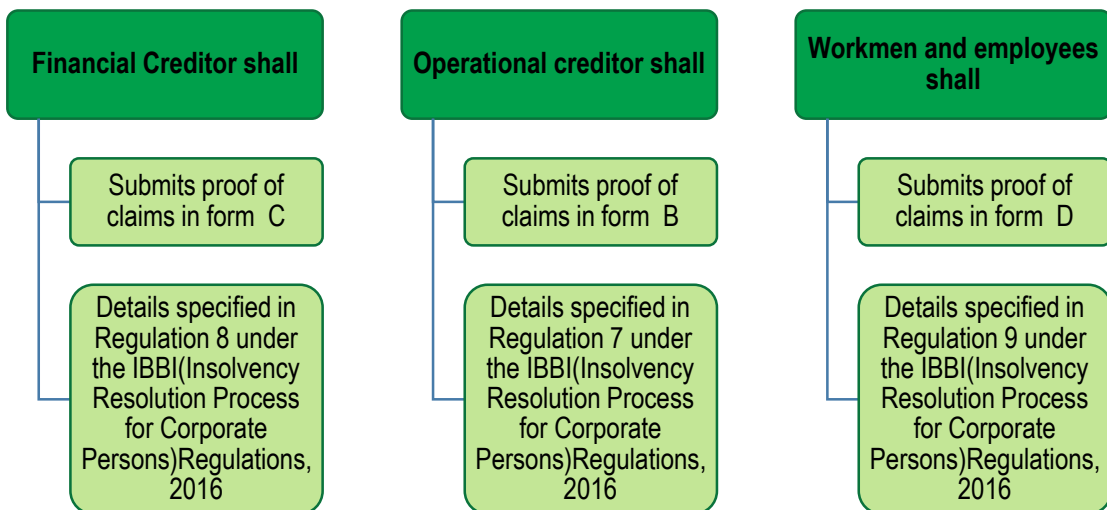
The interim resolution professional shall have the authority—

- (a) to appoint accountants, legal or other professionals as may be necessary;
- (b) to enter into contracts on behalf of the corporate debtor or to amend or modify the contracts or transactions which were entered into before the commencement of corporate insolvency resolution process;
- (c) to raise interim finance provided that no security interest shall be created over any encumbered property of the corporate debtor without the prior consent of the creditors whose debt is secured over such encumbered property:

Provided that no prior consent of the creditor shall be required where the value of such property is not less than the amount equivalent to twice the amount of the debt.

- (d) to issue instructions to personnel of the corporate debtor as may be necessary for keeping the corporate debtor as a going concern; and
 - (e) to take all such actions as are necessary to keep the corporate debtor as a going concern.
- [Section 20]**

Manner of submission of proof of claims to IRP: Proofs of claim shall be committed to IRP as follows:



A creditor shall submit claim with proof on or before the last date mentioned in the public announcement. The IRP shall verify such claims within 7 days from the last date of receipt of the claims and within two days of such verification of claims, file a report to the Adjudicating Authority, certifying constitution of the CoC.

However, a creditor, who fails to submit claim with proof within the time stipulated in the public announcement, may submit the claim with proof to the interim resolution professional or the resolution professional, as the case may be, on or before the ninetieth day of the insolvency commencement date. The IRP or the RP, as the case may be, shall verify every claim and thereupon maintain a list of creditors. Such list of creditors shall be filed with the Adjudicating Authority and also, displayed on the website, if any, of the Corporate Debtor.

(XII) Resolution Professional (RP)

Appointment: As per **Section 22** of the Code, the first meeting of the committee of creditors shall be held within seven days of the constitution of the committee of creditors.

The Committee of Creditors in the first meeting by majority vote of not less than 66% of the Voting Share of the Financial Creditors either-

- **resolve to appoint** the interim resolution professional as a Resolution Professional, or
- **to replace** the interim resolution professional by another Resolution Professional.

Where the committee of creditors resolves—

- (a) **to continue the interim resolution professional as resolution professional** subject to a written consent from the interim resolution professional in the specified form, it shall communicate its decision to the interim resolution professional, the corporate debtor and the Adjudicating Authority; or
- (b) **to replace the interim resolution professional**, it shall file an application before the Adjudicating Authority for the appointment of the proposed resolution professional along with a written consent from the proposed resolution professional in the specified form.

The Adjudicating Authority shall forward the name of the resolution professional proposed to the Board for its confirmation and shall make such appointment after confirmation by the Board.

Where the Board does not confirm the name of the proposed resolution professional within ten days of the receipt of the name of the proposed resolution professional, the Adjudicating Authority shall, by order, direct the interim resolution professional to continue to function as the resolution professional until such time as the Board confirms the appointment of the proposed resolution professional.

Example: Mr. Z was the Interim Resolution Professional (IRP) in XY Company. The committee of creditors by majority vote of financial creditors proposed to appoint Mr. Final as Resolution professional (RP) of the XY Company. The said proposal was confirmed by the Board after 10

days. As per Section 22 of the Code, if Board does not confirm the proposed name as RP within 10 days of receipt of proposal, the Adjudicating authority shall direct IRP i.e., Mr. Z to continue as RP for such time as the Board confirms for the appointment of proposed RP.

Role and Duties of RP: The primary role and duty of RP is to conduct corporate insolvency resolution process and to preserve and protect the assets of the corporate debtor, including the continued business operations of the corporate debtor.

- (1) RP shall conduct the entire corporate insolvency resolution process and manage the operations of the corporate debtor during the corporate insolvency resolution process period.

Provided that the resolution professional shall continue to manage the operations of the corporate debtor after the expiry of the corporate insolvency resolution process period, until an order approving the resolution plan under sub-section (1) of section 31 or appointing a liquidator under section 34 is passed by the Adjudicating Authority.

- (2) RP shall exercise powers and perform duties as are vested or conferred on the interim resolution professional under this Chapter.
- (3) In case of any appointment of a resolution professional other than IRP, the interim resolution professional shall provide all the information, documents and records pertaining to the corporate debtor in his possession and knowledge to the resolution professional. **[Section 23]**

Duties: It shall be the duty of the resolution professional to preserve and protect the assets of the corporate debtor, including the continued business operations of the corporate debtor. The resolution professional shall undertake the following actions to protect the assets of the corporate debtor, namely:—

- (a) take immediate custody and control of all the assets of the corporate debtor, including the business records of the corporate debtor;
- (b) represent and act on behalf of the corporate debtor with third parties, exercise rights for the benefit of the corporate debtor in judicial, quasi-judicial or arbitration proceedings;
- (c) raise interim finances subject to the approval of the committee of creditors;
- (d) appoint accountants, legal or other professionals in the manner as specified by Board;
- (e) maintain an updated list of claims;
- (f) convene and attend all meetings of the committee of creditors;
- (g) prepare the information memorandum;
- (h) invite prospective resolution applicants, who fulfil such criteria as may be laid down by him with the approval of committee of creditors, having regard to the complexity and scale of

operations of the business of the corporate debtor and such other conditions as may be specified by the Board, to submit a resolution plan or plans;

- (i) present all resolution plans at the meetings of the committee of creditors;
- (j) file application for avoidance of transactions in accordance with Chapter III, if any; and
- (k) such other actions as may be specified by the Board. **[Section 25]**

Eligibility of an insolvency Professional to be appointed as a Resolution Professional: As per Regulation 3 of Insolvency and Bankruptcy (Insolvency Resolution process for corporate persons) Regulation, 2016, an insolvency professional shall be eligible for appointment as an interim resolution or a resolution professional for a corporate insolvency process if he and all partners and directors of the insolvency professional entity of which he is partner or director are independent of the corporate debtor:-

- (a) He is eligible to be appointed as an independent director on the board of the corporate debtor under section 149 of the Companies Act, 2013, where the corporate debtor is a company.
- (b) He is not a related party of the corporate debtor.
- (c) He is not an employee or proprietor or a partner of a firm of auditors or secretarial auditors in practice or cost auditors of the corporate debtor in the last three financial years.
- (d) He is not an employee or proprietor or a partner of a legal or consulting firm that has or had any transaction with the corporate debtor amounting to five per cent or more of the gross turnover of such firm in the last three financial years.

Fees of Resolution Professional: As per Section 5(13) of the Code, the fees payable to any person acting as a resolution professional and any costs incurred by the resolution professional in running the business of the corporate debtor as a going concern shall be included in the insolvency resolution process costs and shall be paid in priority before payment to any other creditor. Recently IBBI has come out with the Circular, mandating minimum fees to be paid to the Resolution Professional. (Schedule II of IBBI (IRPCP) Regulations)

Replacement of Resolution Professional: As per the Section 27 of the Code, RP shall be replaced in the following manner:

- If at any time during the Corporate Insolvency Resolution Process the Committee of creditors is of the opinion that the resolution professional appointed is required to be replaced, they may apply to the Adjudicating Authority for replacement of such professional.
- As per Section 27 of the Code, the committee of creditors may, at a meeting, by a vote of sixty-six per cent of voting shares, resolve to replace the resolution professional appointed under section 22 with another resolution professional, subject to a written consent from the proposed resolution professional in the specified form.
- The Committee of Creditors shall forward the name of the new proposed Insolvency

Professional to the Adjudicating Authority, and Adjudicating Authority shall forward such name to the Board for confirmation.

- After the confirmation of the proposed insolvency resolution professional by the Board he shall be appointed in the same manner as laid down in Section 16 which deals with the Appointment of IRP.
- Where any disciplinary proceedings are pending against the proposed resolution professional, the resolution professional appointed under section 22 shall continue till the appointment of another resolution professional.

Preparation of information memorandum: (1) The resolution professional shall prepare an information memorandum containing such relevant information as may be specified by the Board for formulating a resolution plan.

(2) The resolution professional shall provide to the resolution applicant access to all relevant information in physical and electronic form, provided such resolution applicant undertakes—

- (a) to comply with provisions of law for the time being in force relating to confidentiality and insider trading;
- (b) to protect any intellectual property of the corporate debtor it may have access to; and
- (c) not to share relevant information with third parties unless clauses (a) and (b) above are complied with.

"Relevant information" means the information required by the resolution applicant to make the resolution plan for the corporate debtor, which shall include the financial position of the corporate debtor, all information related to disputes by or against the corporate debtor and any other matter pertaining to the corporate debtor as may be specified. **[Section 29]**

(XIII) Committee of Creditors

Constitution of CoC: As per section 21, the **interim resolution professional** shall after collation of all claims received against the corporate debtor and determination of the financial position of the corporate debtor, **constitute a committee of creditors** (CoC).

The committee of creditors shall comprise of all the financial creditors of the corporate debtor.

When FC/ authorized representative is not entitled to participate in the CoC: for the Financial Creditor or the authorised representative of the financial creditor referred to in section 24(6), 24(6A), or 24(5), if it is a related party of the corporate debtor, shall not have any right of representation, participation or voting in a meeting of the committee of creditors:

Provided further that the first proviso shall not apply to a financial creditor, regulated by a financial sector regulator, if it is a related party of the corporate debtor solely on account of conversion or

substitution of debt into equity shares or instruments convertible into equity shares, or completion of such transactions as may be prescribed prior to the insolvency commencement date.

In case where debts owed to two or more FC: The corporate debtor owes financial debts to two or more financial creditors as part of a consortium or agreement, each such financial creditor shall be part of the committee of creditors and their voting share shall be determined on the basis of the financial debts owed to them.

In case, **any person is a financial creditor as well as an operational creditor,—**

- (a) such person **shall be a financial creditor to the extent of the financial debt owed by the corporate debtor**, and shall be included in the committee of creditors, with voting share proportionate to the extent of financial debts owed to such creditor;
- (b) such person **shall be considered to be an operational creditor to the extent of the operational debt owed by the corporate debtor** to such creditor.

Where an operational creditor has assigned or legally transferred any operational debt to a financial creditor, the assignee or transferee shall be considered as an operational creditor to the extent of such assignment or legal transfer.

In case of consortium arrangement of FC: Where the terms of the financial debt extended as part of a consortium arrangement or syndicated facility provide for a single trustee or agent to act for all financial creditors, each financial creditor may—

- (a) Authorise the trustee or agent to act on his behalf in the committee of creditors to the extent of his voting share;
- (b) Represent himself in the committee of creditors to the extent of his voting share;
- (c) Appoint an insolvency professional (other than the resolution professional) at his own cost to represent himself in the committee of creditors to the extent of his voting share; or
- (d) Exercise his right to vote to the extent of his voting share with one or more financial creditors jointly or severally.

Voting by authorised representative of class of FC: As per section 21(6A), if a financial debt is owned by a class of creditors, an insolvency professional can be appointed by adjudicating authority on receipt of application from interim Resolution professional.

Who can act as an authorised representative?

Where a financial debt is in the form of securities or deposits and the terms of the financial debt provide for appointment of a trustee or agent to act as authorised representative for all the financial creditors—

- such trustee or agent shall act on behalf of such financial creditors;

Where a financial debt is owed to a class of creditors other than the creditors covered above, the IRP shall make an application to the AA along with the list of all financial creditors, with the name of an insolvency professional

- to act as their authorised representative appointed by the Adjudicating Authority prior to the first meeting of the committee of creditors;

Where a financial debt is represented by a guardian, executor or administrator,

- such person shall act as authorised representative on behalf of such financial creditors

Authorised Representative from the State or Union Territory having highest number of creditors in class

The Interim Resolution Professional shall offer the names of three insolvency professionals to be voted upon by the class of creditors, who must be from the State or Union Territory, which has the highest number of creditors in the class as per records of the corporate debtor.

Where such State or Union Territory does not have adequate number of insolvency professionals, the insolvency professionals having addresses in a nearby State or Union Territory, as the case may be, shall be considered.

Rights of Authorised representative: Above Authorised representative shall attend the meetings of the committee of creditors, and vote on behalf of each financial creditor to the extent of his voting share.

All decisions of the committee of creditors shall be taken by a vote of not less than fifty-one per cent of voting share of the financial creditors.

Provided that where a corporate debtor does not have any financial creditors, the committee of creditors shall be constituted and shall comprise of such persons to exercise such functions in such manner as may be specified.

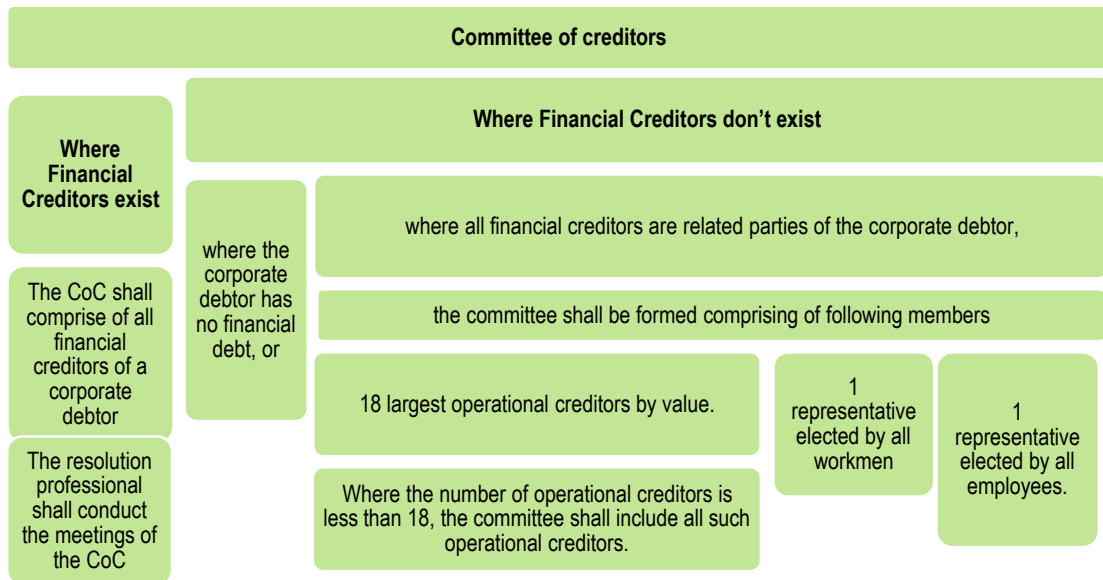
The committee of creditors shall have the right to require the resolution professional to furnish any financial information in relation to the corporate debtor at any time during the corporate insolvency resolution process.

The resolution professional shall make available any financial information so required by the committee of creditors as mentioned above within a period of seven days of such requisition.

(XIII) Meeting of committee of creditors

The provisions related to the meeting of committee of creditors are being dealt under the section 24 of the Code.

Composition: The composition of the committee shall be as follows:-



Procedure for conduct of meeting of CoC: The members of the committee of creditors may meet in person or by such electronic means. All the meeting of CoC shall be conducted by the RP. Notice of meeting shall be served to the following:

- members of Committee of creditors, including the authorised representatives;
- members of the suspended Board of Directors or the partners of the corporate persons, as the case may be;
- operational creditors or their representatives if the amount of their aggregate dues is not less than ten per cent of the debt.

The directors, partners and one representative of operational creditors, as referred above, may attend the meetings of committee of creditors, but shall not have any right to vote in such meetings. The absence of any them shall not invalidate proceedings of such meeting. The resolution professional shall determine the voting share to be assigned to each creditor in the manner specified by the Board.

As per section 5(28) “**voting share**” means the share of the voting rights of a single financial creditor in the committee of creditors which is based on the proportion of the financial debt owed

to such financial creditor in relation to the financial debt owed by the corporate debtor. Each creditor shall vote in accordance with the voting share assigned to him based on the financial debts owed to such creditor. However voting rights of committee with only operational creditor will be in proportion to debt due to each creditor to "total debt". Whereas total debt will be equal to debts due to creditors, workmen and employees. [Regulation 16(3) of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016].

Filing of report certifying constitution of the committee

The interim resolution professional shall file a report certifying constitution of the committee to the Adjudicating Authority within two days of the verification of claims received.

First Meeting of Creditors: The interim resolution professional shall hold the first meeting of the committee within seven days of filing the report as mentioned above.

Where the appointment of resolution professional is delayed, the interim resolution professional shall perform the functions of the resolution professional from the fortieth day of the insolvency commencement date till a resolution professional is appointed under section 22 as per regulation 17 of IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016.

Meetings of the committee

- (1) A resolution professional may convene a meeting of the committee as and when he considers necessary.
- (2) On a request received from members of the committee, shall convene a meeting if the same is made by members of the committee representing thirty three per cent of the voting rights.

Explanation—For the purposes of sub-regulation (2) it is clarified that meeting (s) may be convened under this sub-regulation till the resolution plan is approved under sub-section (1) of section 31 or order for liquidation is passed under section 33 and decide on matters which do not affect the resolution plan submitted before the Adjudicating Authority.

- (3) A resolution professional may place a proposal received from members of the committee in a meeting, if he considers it necessary and shall place the proposal if the same is made by members of the committee representing at least thirty three per cent of the voting rights.

[Regulation 18 of the of IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016]

Notice for meetings of the committee

- (1) A meeting of the committee shall be called by giving not less than five days' notice in writing to every participant,
- (2) The committee may reduce the notice period from five days to such other period of not less than twenty-four hours, as it deems fit:

Provided that the committee may reduce the period to such other period of not less than forty-eight hours if there is any authorised representative. [Regulation 19 of the of IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016.]

Quorum for the Meeting

- A meeting of committee of creditors shall quorate if members of the **committee of creditors representing at least thirty-three percent of the voting rights are present** either in person or by video/audio means. Provided that the committee may modify the percentage of voting rights required for quorum in respect of any future meetings of the committee. [Regulation 22 of the of IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016]
- If the **requisite quorum for committee of creditors is not fulfilled** the meeting cannot be held and the meeting shall automatically stand adjourned at the same time and place on the next day.
- The adjourned meeting shall quorate with the members of the committee attending the meeting.

Approval of committee of creditors for certain actions:

- (1) According to section 28 of the Code, the resolution professional, during the corporate insolvency resolution process, shall not take any of the following actions without the prior approval of the committee of creditors namely:—
 - (a) **raise any interim finance** in excess of the amount as may be decided by the committee of creditors in their meeting;
 - (b) **create any security interest** over the assets of the corporate debtor;
 - (c) **change the capital structure** of the corporate debtor, including by way of issuance of additional securities, creating a new class of securities or buying back or redemption of issued securities in case the corporate debtor is a company;
 - (d) **record any change** in the ownership interest of the corporate debtor;
 - (e) **give instructions** to financial institutions maintaining accounts of the corporate debtor for a debit transaction from any such accounts in excess of the amount as may be decided by the committee of creditors in their meeting;
 - (f) **undertake any related party transaction**;
 - (g) **amend any constitutional documents** of the corporate debtor;
 - (h) **delegate its authority** to any other person;
 - (i) **dispose of or permit the disposal of shares** of any shareholder of the corporate debtor or their nominees to third parties;
 - (j) **make any change in the management** of the corporate debtor or its subsidiary;

- (k) **transfer rights or financial debts or operational debts** under material contracts otherwise than in the ordinary course of business;
 - (l) **make changes in the appointment or terms of contract** of such **personnel** as specified by the committee of creditors; or
 - (m) **make changes in the appointment or terms of contract** of **statutory auditors** or internal auditors of the corporate debtor.
- (2) The resolution professional shall convene a meeting of the committee of creditors and seek the vote of the creditors prior to taking any of the above actions.
 - (3) No action shall be approved by the committee of creditors unless approved by a vote of sixty-six per cent of the voting shares.
 - (4) Where any action is taken by the resolution professional without seeking the approval of the committee of creditors in the manner as required in this section, such action shall be void.
 - (5) The committee of creditors may report the actions of the resolution professional to the Board for taking necessary actions against him under this Code.

Voting by the committee

The resolution professional shall take a vote of the members of the committee present in the meeting, on any item listed for voting after discussion on the same.

At the conclusion of a vote at the meeting, the resolution professional shall announce the decision taken on items along with the names of the members of the committee who voted for or against the decision, or abstained from voting. [Regulation 25 of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016.]

The resolution professional shall provide each member of the committee the means to exercise its vote by either electronic means or through electronic voting system in accordance with the provisions of this Regulation

Rights and duties of authorised representative of financial creditors.

Right to vote and participate to the authorize representative in CoC Meetings: According to Section 25A of the Code, the authorised representative under section 21(6) or 21(6A) or section 24(5) shall have the right to participate and vote in meetings of the committee of creditors on behalf of the financial creditor he represents in accordance with the prior voting instructions of such creditors obtained through physical or electronic means.

To circulate the agenda and minutes: It shall be the duty of the authorised representative to circulate the agenda and minutes of the meeting of the committee of creditors to the financial creditor he represents.

To act in the interest of Financial Creditor: The authorised representative shall not act against the interest of the financial creditor he represents and shall always act in accordance with their prior instructions.

Cast of vote by authorized representative: Provided that if the authorised representative represents several financial creditors, then he shall cast his vote in respect of each financial creditor in accordance with instructions received from each financial creditor, to the extent of his voting share:

Provided further that if any financial creditor does not give prior instructions through physical or electronic means, the authorised representative shall **abstain from voting** on behalf of such creditor.

The authorised representative under section 21(6) shall cast his vote on behalf of all the financial creditors he represents in accordance with the decision taken by a vote of more than fifty per cent, of the voting share of the financial creditors he represents, who have cast their vote.

Provided that for a vote to be cast in respect of an application under section 12 A, the authorised representative shall cast his vote in accordance with the provisions of sub-section (3).

Instruction/ information filed by the authorised representative received by the FC he represents with CoC for voting: The authorised representative shall file with the committee of creditors any instructions received by way of physical or electronic means, from the financial creditor he represents, for voting in accordance therewith, to ensure that the appropriate voting instructions of the financial creditor he represents is correctly recorded by the interim resolution professional or resolution professional, as the case may be.

Explanation.—For the purposes of this section, the "electronic means" shall be such as may be specified.

Voting by Authorised Representative.

The authorised representative shall cast his vote in respect of each financial creditor or on behalf of all financial creditors he represents in accordance with the provisions of sub-section (3) or sub-section (3A) of section 25A, as the case may be. [Regulation 25A of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016.]

(XIV) Persons not eligible to be resolution applicant

One of the key duties of a Resolution professional as per section 25 of the Code is to invite prospective resolution applicants to submit resolution plans for the Corporate Debtor and present all the resolution plans before the Committee of Creditors.

Grounds of ineligibility to be a resolution applicant: Section 29A states that a person shall not be eligible to submit a resolution plan, if such person, or any other person acting jointly or in concert with such person is a/an —

- (a) is an **undischarged insolvent**;
- (b) is a **wilful defaulter** in accordance with the guidelines of the Reserve Bank of India issued under the Banking Regulation Act, 1949;
- (c) at the time of submission of the resolution plan **has an account, or an account of a corporate debtor under the management or control of such person or of whom such person is a promoter**, classified as non-performing asset in accordance with the guidelines of the Reserve Bank of India issued under the Banking Regulation Act, 1949 or the guidelines of a financial sector regulator issued under any other law for the time being in force, and at least a period of one year has lapsed from the date of such classification till the date of commencement of the corporate insolvency resolution process of the corporate debtor:

Exception : Provided that the person shall be eligible to submit a resolution plan if such person makes payment of all overdue amounts with interest thereon and charges relating to non-performing asset accounts before submission of resolution plan:

Provided further that nothing in this clause shall apply to a resolution applicant where such applicant is a financial entity and is not a related party to the corporate debtor.

Explanation I.—For the purposes of this proviso, the expression "**related party**" shall not include a financial entity, regulated by a financial sector regulator, if it is a financial creditor of the corporate debtor and is a related party of the corporate debtor solely on account of conversion or substitution of debt into equity shares or instruments convertible into equity shares, or completion of such transactions as may be prescribed prior to the insolvency commencement date.

Explanation II.—For the purposes of this clause, where a resolution applicant has an account, or an account of a corporate debtor under the management or control of such person or of whom such person is a promoter, classified as non-performing asset and such account was acquired pursuant to a prior resolution plan approved under this Code, then, the provisions of this clause **shall not apply to such resolution applicant for a period of three years** from the date of approval of such resolution plan by the Adjudicating Authority under this Code;

- (d) has been **convicted for any offence** punishable with imprisonment—
 - (i) for two years or more under any Act specified under the Twelfth Schedule; or
 - (ii) for seven years or more under any other law for the time being in force:

Provided that this clause shall not apply to a person after the expiry of a period of two years from the date of his release from imprisonment:

Provided further that this clause shall not apply in relation to a connected person referred to in clause (iii) of Explanation I;]

- (e) is **disqualified to act as a director** under the Companies Act, 2013 (18 of 2013):
Provided that this clause shall not apply in relation to a connected person referred to in clause (iii) of Explanation I;
- (f) is **prohibited by the Securities and Exchange Board of India** from trading in securities or accessing the securities markets;
- (g) has been a promoter or in the management or control of a corporate debtor in which a preferential transaction, undervalued transaction, extortionate credit transaction or fraudulent transaction has taken place and in respect of which an order has been made by the Adjudicating Authority under this Code:
Provided that this clause shall not apply if a preferential transaction, undervalued transaction, extortionate credit transaction or fraudulent transaction has taken place prior to the acquisition of the corporate debtor by the resolution applicant pursuant to a resolution plan approved under this Code or pursuant to a scheme or plan approved by a financial sector regulator or a court, and such resolution applicant has not otherwise contributed to the preferential transaction, undervalued transaction, extortionate credit transaction or fraudulent transaction;
- (h) has **executed a guarantee in favour of a creditor in respect of a corporate debtor** against which an application for insolvency resolution made by such creditor has been admitted under this Code and such guarantee has been invoked by the creditor and remains unpaid in full or part ;
- (i) is subject to **any disability**, corresponding to clauses (a) to (h), under any law in a jurisdiction outside India; or
- (j) has a **connected person** not eligible under clauses (a) to (i).

Explanation I—For the purposes of this clause, the expression "connected person" means—

- (i) any person who is the promoter or in the management or control of the resolution applicant; or
- (ii) any person who shall be the promoter or in management or control of the business of the corporate debtor during the implementation of the resolution plan; or
- (iii) the holding company, subsidiary company, associate company or related party of a person referred to in clauses (i) and (ii):

Provided that nothing in clause (iii) of Explanation I shall apply to a resolution applicant where such applicant is a financial entity and is not a related party of the corporate debtor:

Provided further that the expression "**related party**" shall not include a financial entity, regulated by a financial sector regulator, if it is a financial creditor of the corporate debtor and is a related

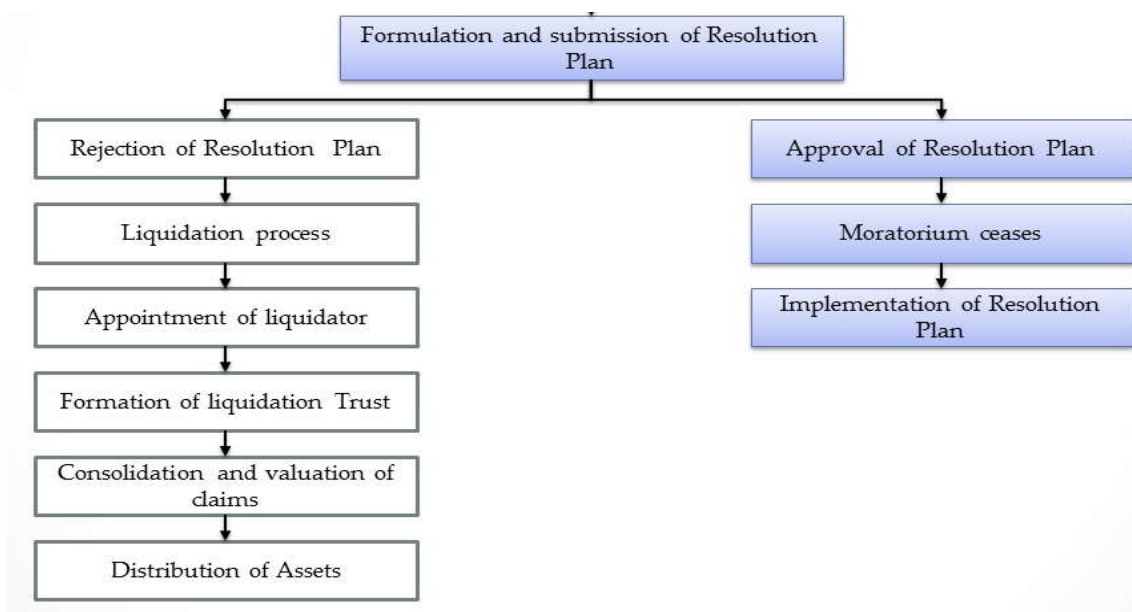
party of the corporate debtor solely on account of conversion or substitution of debt into equity shares or instruments convertible into equity shares, prior to the insolvency commencement date;

Explanation II.—For the purposes of this section, "**financial entity**" shall mean the following entities which meet such criteria or conditions as the Central Government may, in consultation with the financial sector regulator, notify in this behalf, namely:—

- (a) a scheduled bank;
- (b) any entity regulated by a foreign central bank or a securities market regulator or other financial sector regulator of a jurisdiction outside India which jurisdiction is compliant with the Financial Action Task Force Standards and is a signatory to the International Organisation of Securities Commissions Multilateral Memorandum of Understanding;
- (c) any investment vehicle, registered foreign institutional investor, registered foreign portfolio investor or a foreign venture capital investor, where the terms shall have the meaning assigned to them in regulation 2 of the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2017 made under the Foreign Exchange Management Act, 1999;
- (d) an asset reconstruction company registered with the Reserve Bank of India under section 3 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;
- (e) an Alternate Investment Fund registered with the Securities and Exchange Board of India;
- (f) such categories of persons as may be notified by the Central Government.

(XV) Resolution Plan

A resolution plan is defined under section 5(26) "means a plan proposed by resolution applicant for insolvency resolution of the corporate debtor as a going concern in accordance with Part II". It has to be approved by the CoC by a vote of not less than sixty-six per cent of voting share of the CoC members, before being presented to the Adjudicating Authority. The **sections 30 and 31 of the Code** deal with resolution plan. A resolution applicant may submit a resolution plan along with an affidavit stating that he is eligible under section 29A, to the resolution professional prepared on the basis of the information memorandum.



Duty of resolution professional on submission of Resolution plan: The resolution professional shall examine each resolution plan received by him to confirm that each resolution plan—

- (a) Provides the **manner for the payment of insolvency resolution process costs** in priority to the payment of other debts of the corporate debtor;
- (b) provides for the **payment of the debts of operational creditors** as may be specified by the Board which shall not be less than the amount to be paid to the operational creditors in the event of a liquidation of the corporate debtor under section 53; or the amount that would have been paid to such creditors, if the amount to be distributed under the resolution plan had been distributed in accordance with the order of priority in sub-section (1) of section 53

whichever is higher, and provides for the payment of debts of financial creditors, who do not vote in favour of the resolution plan, in such manner as may be specified by the Board, which shall not be less than the amount to be paid to such creditors in accordance with sub-section (1) of section 53 in the event of a liquidation of the corporate debtor.

Explanation 1. — For removal of doubts, it is hereby clarified that a distribution in accordance with the provisions of this clause shall be fair and equitable to such creditors.

Explanation 2. — For the purpose of this clause, it is hereby declared that on and from the date of commencement of the Insolvency and Bankruptcy Code (Amendment) Act, 2019, the provisions of this clause shall also apply to the corporate insolvency resolution process of a corporate debtor-

- i. where a resolution plan has not been approved or rejected by the Adjudicating Authority;
 - ii. where an appeal has been preferred under section 61 or section 62 or such an appeal is not time barred under any provision of law for the time being in force; or
 - iii. where a legal proceeding has been initiated in any court against the decision of the Adjudicating Authority in respect of a resolution plan;
- (c) provides for the management of the affairs of the Corporate Debtor after approval of the resolution plan;
- (d) the implementation and supervision of the resolution plan;
- (e) does not contravene any of the provisions of the law for the time being in force.
- (f) Conforms to such other requirements as may be specified by the Board.

Seeking approval of CoC: The resolution professional shall present such resolution plans, that satisfy the aforementioned conditions, to the committee of creditors for its approval by a vote of not less than sixty-six per cent of voting share of the financial creditors after considering its feasibility and viability, the manner of distribution proposed, which may take into account the order of priority amongst creditors as laid down in sub-section (1) of section 53, including the priority and value of the security interest of a secured creditor and such other requirements as may be specified by the Board. (Sec 30(3) and (4))

Provided that the committee of creditors shall not approve a resolution plan, submitted before the commencement of the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2017, where the resolution applicant is ineligible under section 29A and may require the resolution professional to invite a fresh resolution plan where no other resolution plan is available with it.

Provided further that where the resolution applicant referred to in the first proviso is ineligible under clause (c) of section 29A, the resolution applicant shall be allowed by the committee of creditors thirty days, to make payment of overdue amounts in accordance with the proviso to clause (c) of section 29A.

Provided also that nothing in the second proviso shall be construed as extension of period for the purposes of the proviso to section 12(3), and the corporate insolvency resolution process shall be completed within the period specified in that sub-section.

Provided also that the eligibility criteria in section 29A as amended by the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2018 shall apply to the resolution applicant who has not submitted resolution plan as on the date of commencement of the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2018.

Attending of meeting by resolution applicant: The resolution applicant may attend the meeting of the committee of creditors in which the resolution plan of the applicant is considered.

Provided that the resolution applicant shall not have a right to vote at the meeting of the committee of creditors unless such resolution applicant is also a financial creditor.

Voting on resolution plan: The committee of creditors shall-

- (a) evaluate the resolution plans as per evaluation matrix;
- (b) record its deliberations on the feasibility and viability of each resolution plan; and
- (c) vote on all such resolution plans simultaneously.

Where only one resolution plan is put to vote, it shall be considered approved if it receives requisite votes. Where two or more resolution plans are put to vote simultaneously, the resolution plan, which receives the highest votes, but not less than requisite votes, shall be considered as approved.

Provided that where two or more resolution plans receive equal votes, but not less than requisite votes, the committee shall approve any one of them, as per the tie-breaker formula announced before voting.

Provided further that where none of the resolution plans receives requisite votes, the committee shall again vote on the resolution plan that received the highest votes, subject to the timelines under the Code. (Reg 39(3B))

Submission of the resolution plan: The resolution professional shall submit the resolution plan as approved by the committee of creditors to the Adjudicating Authority. **[Section 30]**

Approval of resolution plan: If the Adjudicating Authority is satisfied that the resolution plan as approved by the committee of creditors meets the requirements as per section 30(2), it shall by order approve the resolution plan which shall be binding on the following:

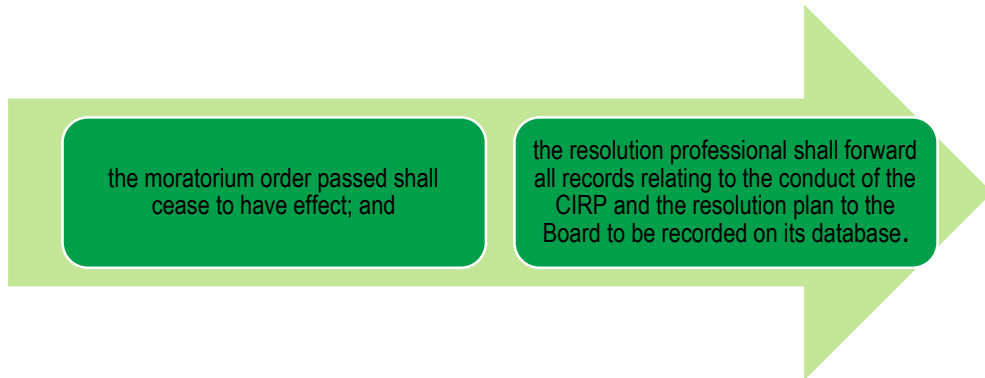
- corporate debtor and its employees,
- members, creditors, guarantors, and
- other stakeholders involved in the resolution plan
- Central Government, State Government and Local Authority

Case Law

SC in *Committee of Creditors of Essar Steel India Ltd. Vs. Satish Kumar Gupta & Ors.* Civil Appeal No. 8766-67 of 2019 dated 15th November 2019 it was decided that the successful resolution applicant does on a fresh slate, and all the liabilities get extinguished on approval of the resolution plan beyond what has been part of the plan.

Rejection of the resolution plan: Where the Adjudicating Authority is satisfied that the resolution plan does not conform to the above requirements, it may, by an order, reject the resolution plan.

Consequences of approval: After the order of approval,—



The resolution applicant shall obtain the necessary approval pursuant to the resolution plan approved, within a period of one year from the date of approval of the resolution plan by the Adjudicating Authority or within such period as provided for in such law, whichever is later.

Provided that where the resolution plan contains a provision for combination, as per section 5 of the Competition Act, 2002, the resolution applicant shall obtain the approval of the Competition Commission of India under that Act prior to the approval of such resolution plan by the committee of creditors. **[Section 31]**

Case Law

Supreme Court in the matter of *K. Sashidhar Vs. Indian Overseas Bank & Ors.* in Civil Appeal No. 10673 of 2018, C.A. No.10719 of 2018, 10971 of 2018 and SLP (C) No.29181 of 2018 dt 5 Feb 2019 it was decided that No provision has been envisaged by the legislature to empower the RP, the NCLT or NCLAT, to reverse the commercial decision of the CoC

Liabilities for previous offences:

(1) **Liability of a Corporate Debtor for an offence committed prior to the commencement of the corporate insolvency resolution process:** Notwithstanding anything to the contrary contained in this Code or any other law for the time being in force, the liability of a corporate debtor for an offence committed prior to the commencement of the corporate insolvency resolution process **shall cease**, and the corporate debtor shall not be prosecuted for such an offence from the date the resolution plan has been approved by the Adjudicating Authority under section 31, if the resolution plan results in the change in the management or control of the corporate debtor to a person who was not-

- a) a promoter or in the management or control of the corporate debtor or a related party of such a person; or
- b) a person with regard to whom the relevant investigating authority has, on the basis of material in its possession, reason to believe that he had abetted or conspired for the

commission of the offence, and has submitted or filed a report or a complaint to the relevant statutory authority or Court:

Provided that if a prosecution had been instituted during the corporate insolvency resolution process against such corporate debtor, it shall stand discharged from the date of approval of the resolution plan subject to requirements of this sub-section having fulfilled:

Provided further that every person who was a “designated partner” as defined in clause (j) of section 2 of the Limited Liability Partnership Act, 2008 or an “officer who is in default”, as defined in clause (60) of section 2 of the Companies Act, 2013, or was in any manner in-charge of, or responsible to the corporate debtor for the conduct of its business or associated with the corporate debtor in any manner and who was directly or indirectly involved in the commission of such offence as per the report submitted or complaint filed by the investigating authority, shall continue to be liable to be prosecuted and punished for such an offence committed by the corporate debtor notwithstanding that the corporate debtor’s liability has ceased under this sub-section.

(2) **When no action against the property of the corporate debtor shall be taken:** No action shall be taken against the property of the corporate debtor in relation to an offence committed prior to the commencement of the corporate insolvency resolution process of the corporate debtor, **where such property is covered under a resolution plan approved by the Adjudicating Authority under section 31**, which results in the change in control of the corporate debtor to a person, or sale of liquidation assets under the provisions of Chapter III of Part II of this Code to a person, who was not –

- (a) a promoter or in the management or control of the corporate debtor or a related party of such a person; or
- (b) a person with regard to whom the relevant investigating authority has, on the basis of material in its possession, reason to believe that he had abetted or conspired for the commission of the offence, and has submitted or filed a report or a complaint to the relevant statutory authority or Court

(3) Subject to the provisions contained in sub-sections (1) and (2), and notwithstanding the immunity given in this section, the corporate debtor and any person, who may be required to provide assistance under such law as may be applicable to such corporate debtor or person, shall extend all assistance and co-operation to any authority investigating an offence committed prior to the commencement of the corporate insolvency resolution process. [Section 32A]

Appeal against Approval of Resolution Plan: Any appeal from an order approving the resolution plan shall be in the manner and on the grounds laid down in sub-section (3) of section 61.

As per Section 61(3) of the Code, an appeal against an order of Adjudicating Authority for approving the resolution plan may be filed on the following grounds:-

- (a) The approved resolution plan is in contravention of the provisions of any law for the time being in force.
- (b) There has been material irregularity in exercise of the powers by the resolution professional during the corporate insolvency resolution period.
- (c) The debts owed to operational creditors of the corporate debtor have not been provided for in the resolution plan in the manner specified by the Board.
- (d) The insolvency resolution process costs have not been provided for repayment in priority to all other debts.
- (e) The resolution plan does not comply with any other criteria specified by the Board.

Consequences of non-submission of a Resolution Plan: When the Resolution Plan is not filed within 180 days of the Commencement date or such other extended period the Adjudicating Authority may pass orders for the liquidation of the corporate debtor.

Vide Circular No. IBBI/CIRP/41/2021, DATED 18-3-2021, under Regulation 40A of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 ('CIRP regulations') provides a model timeline for carrying out various activities envisaged in a corporate insolvency resolution process (CIRP).

Regulation 40B of the CIRP regulations require an interim resolution professional (IRP)/ resolution professional (RP) to file a set of forms (CIRP 1 to CIRP 6) within seven days of completion of specific activities to enable monitoring progress of CIRP. This implies that a Form (CIRP 1 to CIRP 6) would not be filed until the related activity is not completed for whatever reason. This makes monitoring of progress difficult. Regulation 40B of CIRP regulations require filing of Form CIRP 7 within three days of due date of completion of any activity stated in column (2) of the table below is delayed, and continue to file Form CIRP 7 every 30 days, until the said activity remains incomplete.

<i>Sl. No.</i>	<i>Activity requiring filing of Form CIRP 7, if not completed by the specified date</i>	<i>Timeline for filing Form CIRP 7 for the first time</i>	<i>Timeline for subsequent filing of Form CIRP 7</i>
<i>(1)</i>	<i>(2)</i>	<i>(3)</i>	<i>(4)</i>
<i>1</i>	<i>Public announcement is not made by T+3rd day</i>	<i>Date specified in column (2) + 3 days</i>	<i>X+30th day, X+60th day, X+90th day, and so on, till the activity is completed.</i>
<i>2</i>	<i>Appointment of RP is not made by T+30th day</i>		
<i>3</i>	<i>Information memorandum is not issued within 51 days</i>		

	<i>from the date of public announcement</i>		
4	<i>RFRP is not issued within 51 days from the date of issue of information memorandum</i>		
5	<i>CIRP is not completed by T+180th day</i>		

T = Insolvency commencement date, and

X = Date of filing of Form CIRP 7 for the first time under column (3).

This circular is applicable for all the processes ongoing as on the date of this circular.



4. LIQUIDATION PROCESS

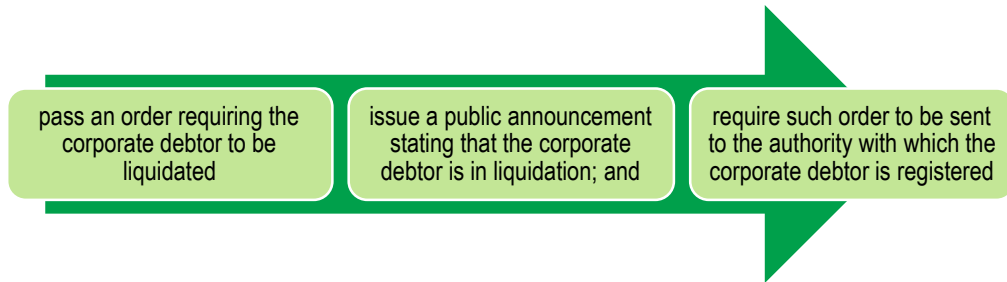
The Code concerns itself only with those corporate debtors which have defaulted in payment of debts. The corporate debtor, at the first stage, is put into resolution mode. The process is called the corporate insolvency resolution process. However, if attempts to resolve the insolvency of the corporate debtor fail, then only the liquidation provisions of the Code are triggered.

Where no plan is received during the CIRP period or where the plan presented is rejected by the Committee of Creditors or if the plan is not approved by the Adjudicating Authority, the Adjudicating Authority shall pass an order requiring the Corporate Debtor to be liquidated in the manner as laid down in Chapter III of the Act. CIRP always precedes Liquidation Process. There is no provision under the Code for direct Liquidation without undergoing CIRP.

Initiation of Liquidation process:

Section 33 of the Code provides that where the Adjudicating Authority, —

- (a) **Not received a Resolution plan:** Before the expiry of the insolvency resolution process period or the maximum period permitted for completion of the corporate insolvency resolution process or the fast track corporate insolvency resolution process, as the case may be, does not receive a resolution plan; or
- (b) **rejects the resolution plan** for the non-compliance of the requirements specified therein, it shall—



Intimation of the decision of the committee of creditors to liquidate to Adjudicating authority:

Where the resolution professional, at any time during the corporate insolvency resolution process but before confirmation of resolution plan, intimates the Adjudicating Authority of the decision of the committee of creditors approved by not less than sixty-six per cent of the voting share to liquidate the corporate debtor, the Adjudicating Authority shall pass a liquidation order.

Contravention of resolution plan as approved by the Adjudicating Authority: Where the resolution plan approved by the Adjudicating Authority under section 31 or under sub-section (1) of section 54L, is contravened by the concerned corporate debtor, any person other than the corporate debtor, whose interests are prejudicially affected by such contravention, may make an application to the Adjudicating Authority for a liquidation order.

Determination of contravention of the provisions of the resolution plan: On receipt of an application, if the Adjudicating Authority determines that the corporate debtor has contravened the provisions of the resolution plan, it shall pass a liquidation order.

Bar to filing of suits and legal proceedings: Subject to section 52, when a liquidation order has been passed, no suit or other legal proceeding shall be instituted by or against the corporate debtor. A suit or other legal proceeding may be instituted by the liquidator, on behalf of the corporate debtor, with the prior approval of the Adjudicating Authority.

Exception: Restrictions on filing of suits and legal proceedings shall not apply to legal proceedings in relation to such transactions as may be notified by the Central Government in consultation with any financial sector regulator.

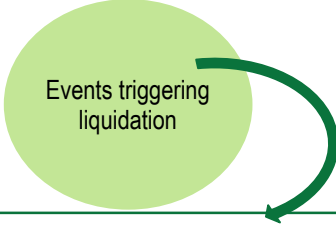
Order to be deemed to be notice of discharge: The order for liquidation under this section shall be deemed to be a notice of discharge to the officers, employees and workmen of the corporate debtor, except when the business of the corporate debtor is continued during the liquidation process by the liquidator.

So, from above it can be concluded that under the Code, a corporate debtor may be put into liquidation in the following scenarios:

- (i) Non-receipt of resolution plan during CIRP period;
- (ii) A 66% majority of the creditor's committee resolves to liquidate the corporate debtor at any time during the insolvency resolution process before confirmation of the resolution plan;

- (iii) The creditor's committee does not approve a resolution plan within 180 days (or within the extended 90 days);
- (iv) The NCLT rejects the resolution plan submitted to it on technical grounds; or
- (v) The debtor contravenes the agreed resolution plan and an affected person makes an application to the NCLT to liquidate the corporate debtor.

Once the NCLT passes an order of liquidation, a moratorium is imposed on the pending legal proceedings against the corporate debtor, and the assets of the debtor (including the proceeds of liquidation) vest in the liquidation estate.



Events triggering liquidation

- On rejection of resolution plan
- Adjudicating Authority does not receive a Resolution Plan on or before the expiry of the maximum time permitted for resolution
- Corporate debtor contravenes the Resolution Plan approved by AA, and any other person being prejudicially affected applies against such contravention
- Creditors' Committee decides to liquidate the corporate debtor at any time during insolvency process, before confirmation of any Resolution Plan

Case Law:

National Company Law Appellate Tribunal, New Delhi, in *Sreedhar Tripathy v. Gujarat State Financial Corporation*, 2022 gave the verdict that where corporate debtor was not functioning for last 19 years and all machinery had become scrap and CoC in its commercial wisdom decided to liquidate corporate debtor, impugned order passed by NCLT directing liquidation of corporate debtor was not to be interfered with.

In the given case, NCLT directed for liquidation of corporate debtor. Here Appellant challenged said order on ground that CoC never wanted to continue with CIRP and decision taken by CoC for liquidation of corporate debtor was not in its commercial wisdom. It was noted that corporate debtor was not functional and was completely shut for last 19 years.

It was held that CoC in its Legislative scheme has been empowered to take decision to liquidate corporate debtor, any time after its constitution and before confirmation of resolution plan. As corporate debtor had not been functioning for last 19 years and all machinery had become scrap, even buildings were in broken-down condition and CIRP would involve huge costs, decision taken by CoC to liquidate corporate debtor was not arbitrary and same was not open for Judicial review by NCLT.

TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. *An application under Section 9 of the Insolvency and Bankruptcy Code, 2016 was filed by the Raheja Portland Cement Limited in the capacity as operational creditor against the corporate debtor Makhija Builders and Developers Limited. The application was admitted by the order of the National Company Law Tribunal – Mumbai (NCLT, Mumbai) after giving a reasonable opportunity of being heard to Makhija Builders and Developers Limited and Mr. Ritesh was appointed as Interim Resolution Professional (IRP). However, Mr. Sanskar and Mr. Satvik, two of the directors of Makhija Builders and Developers Limited, were suspicious about the claims filed by Raheja Portland Cement Limited since they were much more than what was due to the company and therefore, they are desirous of making an appeal against the order of the NCLT, Mumbai. You, as a legal advisor, are required to advise them as to the maximum time within which an appeal against the order of the NCLT, Mumbai, can be filed by them with the National Company Law Appellate Tribunal (NCLAT).*
 - (a) *Mr. Sanskar and Mr. Satvik, the two directors of Makhija Builders and Developers Limited shall be able to prefer an appeal against the order passed by NCLT, Mumbai under Section 9 of the Insolvency and Bankruptcy Code, 2016, within a period of 45 days from the date of order.*
 - (b) *Mr. Sanskar and Mr. Satvik, the two directors of Makhija Builders and Developers Limited shall be able to prefer an appeal against the order passed by NCLT, Mumbai under Section 9 of the Insolvency and Bankruptcy Code, 2016, within a period of 30 days from the date of order.*
 - (c) *Mr. Sanskar and Mr. Satvik, the two directors of Makhija Builders and Developers Limited shall be able to prefer an appeal against the order passed by NCLT, Mumbai under Section 9 of the Insolvency and Bankruptcy Code, 2016, within a period of 15 days from the date of order.*
 - (d) *Mr. Sanskar and Mr. Satvik, the two directors of Makhija Builders and Developers Limited shall be able to prefer an appeal against the order passed by NCLT, Mumbai under Section 9 of the Insolvency and Bankruptcy Code, 2016, within a period of 10 days from the date of order.*
2. *Aakansha Plastics Limited, having registered office at Bhatinda, Punjab, was formed in the year 2005. On March 31, 2021, its paid-up share capital was ₹ 5,00,00,000; Amount due from Debtors viz. Shilpa Furnitures Private Limited and Shobhna Traders & Co. ₹ 4,00,00,000; Secured loans obtained from Crescent Bank Limited ₹ 6,00,00,000; Amount due to creditors, namely, Sambhav & Sons and Satyadev Suppliers Private Limited ₹ 3,00,00,000. The performance of the company decreased sharply due to stiff competition, wrong planning and*

mismanagement and it came on the verge of insolvency. Choose from the following alternatives as to who is the corporate debtor:

- (a) Shilpa Furnitures Private Limited and Shobhna Traders & Co.
 - (b) Aakansha Plastics Limited.
 - (c) Sambhav & Sons and Satyadev Suppliers Private Limited.
 - (d) Crescent Bank Limited.
3. *Ruby Petals Limited, a small company, files an application with the National Company Law Tribunal (NCLT) stating that the fast track corporate insolvency resolution process against it cannot be completed within the prescribed period of 90 days. On being satisfied, NCLT orders to extend the period of such process by 30 days. However, Ruby Petals Limited again initiates an application for further extension of time period of insolvency process by another 10 days. From the four options given below which one, do you think, is applicable in such a situation:*
- (a) *National Company Law Tribunal can extend the period of fast track corporate insolvency resolution process against Ruby Petals Limited by another 10 days since total extension does not exceed 45 days.*
 - (b) *National Company Law Tribunal can extend the period of fast track corporate insolvency resolution process against Ruby Petals Limited by another 10 days if the corporate debtor deposits ₹ 50,000 as penalty.*
 - (c) *National Company Law Tribunal can extend the period of fast track corporate insolvency resolution process against Ruby Petals Limited by another 10 days if the corporate debtor deposits ₹ 1,00,000 as penalty.*
 - (d) *National Company Law Tribunal cannot extend the period of fast track corporate insolvency resolution process against Ruby Petals Limited by another 10 days since such extension shall not be granted more than once.*
4. *Munikh Hospitality Services Limited was admitted in the Corporate Insolvency Resolution Process (CIRP) under Section 7 of the Insolvency and Bankruptcy Code. The Resolution Professional (RP) Mr. Somesh, after his appointment, conducted a meeting of Committee of Creditors (CoC) but the same was adjourned due to the lack of quorum. At the appointed date and time, when the adjourned meeting was resumed, a resolution was passed by the CoC members present, representing 51% of the voting rights, for liquidation of Munikh Hospitality Services Limited, the Corporate Debtor, before the completion of the Corporate Insolvency Resolution Process (CIRP). You, as a qualified Chartered Accountant comprising the team of RP, are required to advise whether the resolution of liquidation passed by certain members of CoC representing 51% of the voting rights is valid or not considering the applicable provisions of the Insolvency and Bankruptcy Code, 2016.*

- (a) *The resolution of liquidation of Munikh Hospitality Services Limited passed by certain members of CoC representing 51% of the voting rights is not valid since the resolution has not been approved by minimum of 90% of the voting shares of the creditors.*
 - (b) *The resolution of liquidation of Munikh Hospitality Services Limited passed by certain members of CoC representing 51% of the voting rights is not valid since the resolution has not been approved by minimum of 66% of the voting shares of the creditors.*
 - (c) *The resolution of liquidation of Munikh Hospitality Services Limited passed by certain members of CoC representing 51% of the voting rights is not valid since such resolution cannot be passed before the completion of the CIRP.*
 - (d) *The resolution of liquidation of Munikh Hospitality Services Limited passed by certain members of CoC representing 51% of the voting rights is valid since the same has been passed by the majority of creditors.*
5. *Shivdeep submitted his claim as an operational creditor to the liquidator of Chiranjeevi Food Products Limited which is under liquidation. After submission of his claim, Shivdeep is desirous of altering it. Out of the following four options, which one correctly indicates the time period within which he can alter his claim after its submission.*
- (a) *Shivdeep can alter his claim within five days of its submission to the liquidator of Chiranjeevi Food Products Limited.*
 - (b) *Shivdeep can alter his claim within ten days of its submission to the liquidator of Chiranjeevi Food Products Limited.*
 - (c) *Shivdeep can alter his claim within fourteen days of its submission to the liquidator of Chiranjeevi Food Products Limited.*
 - (d) *Shivdeep can alter his claim within thirty days of its submission to the liquidator of Chiranjeevi Food Products Limited.*

Descriptive Questions

1. *When will the provisions of insolvency and liquidation be applicable to a corporate person?*
2. *What is the Insolvency Resolution Process for financial creditors?*
3. *What is the Insolvency Resolution Process for operational creditors?*
4. *What are the eligibility criteria for appointment of an Insolvency Professional as a Resolution Professional for a corporate insolvency resolution process?*
5. *What is the procedure of Insolvency Resolution Process for a Corporate Applicant?*
6. *Is there any time limit for completion of the Insolvency Resolution Process?*
7. *What is the effect of order of moratorium?*

8. What is a Resolution plan?
9. What is the significance of the Corporate Insolvency Resolution Commencement Date?
10. Mr. Ram, an operational creditor filed an application for corporate insolvency resolution process. He did not propose for the appointment of an interim resolution professional in the application. State the provisions given by the Code to resolve such a scenario including the term of IRP so appointed.

ANSWERS

Answer to Multiple Choice Questions

1.	b	2.	b	3.	d	4.	b	5.	c

Answer to Descriptive Answers

1. The provisions relating to the insolvency and liquidation of corporate debtors shall be applicable only when the amount of the default is one lakh rupees or more. However, the Central Government may, by notification, specify the minimum amount of default of higher value which shall not be more than one crore rupees.

Vide Notification No. S.O.1205(E), date 24-03-22, minimum amount of default is increase to 1 crore for triggering CIRP under the IBC.

2. A financial creditor either itself or along with other financial creditors may lodge an application before the Adjudicating Authority (National Company Law Tribunal) for initiating corporate insolvency resolution process against a corporate debtor who commits a default in payment of its dues.

The financial creditor shall along with the application give evidence in support of the default committed by the corporate debtor. He shall also give the name of the interim resolution professional.

Where the Adjudicating Authority is satisfied that a default has occurred and the application by the financial creditor is complete and there are no disciplinary proceedings pending against the proposed resolution professional, it may admit such application made by the financial creditor.

If the Adjudicating Authority is satisfied that default has not occurred (reasons to be recorded in writing) or the application is incomplete or any disciplinary proceeding is pending against the resolution professional, it shall reject the application. However, the applicant may rectify the defect within seven days of receipt of notice of rejection from the Adjudicating Authority.

3. On the occurrence of default, an operational creditor shall first send a demand notice and a copy of invoice to the corporate debtor.

The corporate debtor shall within a period of ten days of receipt of demand notice notify the operational creditor about the existence of a dispute, if there is any and record of pendency of any suit or arbitration proceedings. He shall also provide the details of repayment of unpaid operational debt in case the debt has or is being paid.

After the expiry of ten days, if the operational creditor does not receive his payment or the confirmation of a dispute that existed even before the demand notice was sent, he may file an application before the Adjudicating Authority for initiating a corporate insolvency resolution process.

The Adjudicating Authority shall within fourteen days of receipt of the application, admit or reject the application. However, before rejecting the application, an opportunity shall be given to the applicant to rectify the defect within seven days of receipt of rejection.

4. As per Regulation 3 of Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016, an insolvency professional shall be eligible for appointment as a resolution professional for a corporate insolvency resolution process if he and all partners and directors of the insolvency professional entity of which he is partner or director are independent of the corporate debtor i.e.,

- He is eligible to be appointed as an independent director on the board of the corporate debtor under Section 149 of the Companies Act, 2013, where the corporate debtor is a company.
- He is not a related party of the corporate debtor.
- He is not an employee or proprietor or a partner of a firm of auditors or secretarial auditors in practice or cost auditors of the corporate debtor in the **last three financial years**.
- He is not an employee or proprietor or a partner of a legal or consulting firm that has or had any transaction with the corporate debtor amounting to **five per cent** or more of the gross turnover of such firm in the **last three financial years**.

5. Where a corporate debtor has committed a default, a corporate applicant thereof may file an application for initiating corporate insolvency resolution process with the Adjudicating Authority.

The corporate applicant shall furnish the information relating to books of account and other documents and a resolution professional shall be appointed as interim resolution professional.

The Adjudicating Authority may either accept or reject the application within fourteen days of receipt of application. However, applicant shall be allowed to rectify the defect within seven days of receipt of notice of such rejection.

6. Section 12 states that any Insolvency Resolution Process shall be completed within a period of one hundred and eighty days from the date of admission of the application to initiate the process.

However, the National Company Law Tribunal (NCLT) may on an application made by the resolution professional, under a resolution passed by the Committee of Creditors, by a vote of 66% of voting shares, after consideration provide one extension which shall not extend more than 90 days.

Second proviso to Section 12 (3) states that the corporate insolvency resolution process (CIRP) shall compulsorily be completed within **330 days** from the insolvency commencement date including any extension of the time period of corporate insolvency resolution process granted under Section 12 and also the time taken in legal proceedings in relation to such resolution process of the corporate debtor.

7. Section 14 contains the provisions relating to moratorium. During the moratorium period the following acts shall be prohibited:

- (a) The institution of suits or continuation of any pending suits or proceedings against the corporate debtor including execution of any judgment, decree or order in any court of law, tribunal, arbitration panel or other authority;
- (b) Transferring, encumbering, alienating or disposing of by the corporate debtor any of its assets or any legal right or beneficial interest therein;
- (c) Any action to foreclose, recover or enforce any security interest created by the corporate debtor in respect of its property including any action under the SARFAESI Act, 2002
- (d) The recovery of any property by an owner or lessor where such property is occupied by or in the possession of the corporate debtor.

Explanation to Section 14 (1) clarifies that notwithstanding anything contained in any other law for the time being in force, a licence, permit, registration, quota, concession, clearance or a similar grant or right given by the Central Government, State Government, local authority, sectoral regulator or any other authority constituted under any other law for the time being in force, **shall not be suspended or terminated on the grounds of insolvency**, subject to the condition that there is no default in payment of current dues arising for the use or continuation of the license or a similar grant or right during moratorium period.

8. According to Section 5 (26), a 'resolution plan' means a plan proposed by resolution applicant for insolvency resolution of the corporate debtor as a going concern in accordance with Part II of the Code.

Explanation to Section 5 (26) clarifies that a resolution plan may include provisions for the restructuring of the corporate debtor, including by way of merger, amalgamation and demerger.

The aim of the Code is to revive the corporate debtor and therefore, resolution plan should be such that it is capable of resolving the insolvency of the corporate debtor as a going concern.

As per Section 30, the resolution applicant shall prepare resolution plan on the basis of information memorandum and submit the same to the resolution professional.

Each Resolution Plan shall be examined by the resolution professional to confirm that each such plan:

- (i) provides for payment of insolvency resolution costs;
- (ii) provides for repayment of the debts to operational creditors;
- (iii) provides for management of affairs of the company after approval of the resolution plan;
- (iv) provides for implementation and supervision of the resolution plan;
- (v) does not contravene provisions of the law for the time being in force; and
- (vi) conforms to such other requirement as may be specified by the Board.

The resolution plan needs to be submitted within the prescribed time as provided by Section 12. The prescribed time limit is 180 days and in case of extension it is 270 days. Further, 330 days have also been mandated which shall include any extension of the time period of corporate insolvency resolution process granted under Section 12 and also the time taken in legal proceedings in relation to such resolution process of the corporate debtor.

In case of Fast Track Resolution, the time limit is 90 days and if extension is required, another 45 days can be granted.

The resolution professional shall submit the resolution plan to the committee of creditors for its approval which may approve the plan by a vote of not less than 66% of voting share of the financial creditors. Operational creditors have no say in approving the resolution plan.

The resolution professional shall submit the approved plan to the Adjudicating Authority.

9. The commencement date of the corporate insolvency resolution is the beginning of moratorium or a calm period till the completion of the corporate insolvency resolution process during which all suits and legal proceedings etc. against the Corporate Debtor are held in abeyance to give time to the entity to resolve its status.
10. **Appointment of IRP:** As per Section 16 of the Code where the application for corporate insolvency resolution process is made by an operational creditor and no proposal for an interim resolution professional is made in the said application, the Adjudicating Authority shall make a reference to the Board (IBBI) for the recommendation of an insolvency professional who may act as an interim resolution professional.

The Board (IBBI) shall recommend the name of an insolvency professional to the Adjudicating Authority against whom no disciplinary proceedings are pending, within ten days of the receipt of a reference from the Adjudicating Authority.

Period of appointment of IRP: the term of the Interim Resolution Professional shall continue from his appointment till the date of appointment of the Resolution Professional by COC in its first meeting under Section 22 of the Code.

[illegible]