

**PAPER- 4 – CORPORATE AND ECONOMIC LAWS**

Question No. 1 is compulsory.

Answer any **four** from the rest

**Question 1**

(A) You are the CFO and in-charge of legal compliances of large multi-national company in India. The Board of Directors of the Company are broad based and comprise of competent 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) If the original director joins the Board Meeting through video conferencing without returning to India, then, can the alternate director appointed in his place attend the same board meeting? If yes, whose presence and vote will be counted?
- (c) 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?
- (d) Can an Executive Director/Whole Time Director/Managing Director appoint alternate directors? **(8 Marks)**

(B) The Articles of Association of M/s. DEF Limited (Non-Government Company) restricts the Company to contribute to National Defence Fund in any financial year for a sum not exceeding ₹ 5 lakhs. The Articles is silent about contribution to bonafide Charitable Fund and to a Political Party. The Company earned net profit during the last five financial years as under:

<b>Financial Year</b>	<b>Net Profit (₹ in Lakhs)</b>
2018-19	45
2017-18	25
2016-17	20
2015-16	15
2014-15	10

The Board of Directors proposes to contribute in July 2019 for the first time during the financial year 2019-20:

- (i) ₹ 7 Lakhs to National Defence Fund
- (ii) ₹ 3 Lakhs to a bonafide Charitable Fund
- (iii) ₹ 5 Lakh to a Political Party

The Company Seeks your advice on the following matters in respect of each of the above proposals under the provisions of the Companies Act, 2013.

- (i) The appropriate approving authority;
- (ii) The quantum of contribution that can be made;
- (iii) The mode of payment of such contribution

(6 Marks)

**Answer**

- (A) (a) 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 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) The office of alternate director is separate from the attendance of the original director in the Board Meeting and as per section 161(2) of the Companies Act, 2013, an alternate director is appointed to hold the office of original director during his absence from India. Accordingly, as far as attendance in Board Meeting by the original director is concerned, an alternate director may continue to hold office even if the original director joins the meeting by video conferencing, but the original director will be deemed to have joined only as a invitee and the attendance of the alternate director shall be counted for the purpose of the Board Meeting. This is specific only with respect to matters which shall not be dealt with through video conferencing. In such matters where video conferencing is allowed, voting of original director will be counted.
- (c) 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.

- (d) 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 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.

**(B) (i) Appropriate approving authority**

- (a) **In case of National Defence Fund:** As per section 183(1), the Board of Directors of any company or any person or authority exercising the powers of the Board of Directors of a company, or of the company in general meeting, may, contribute such amount as it thinks fit to the National Defence Fund or any other Fund approved by the Central Government for the purpose of national defence.
- (b) **In case of Bonafide Charitable Fund:** As per section 181(1), the Board of Directors of a company may contribute to *bona fide* charitable and other funds. However, prior permission of the company in general meeting shall be required for such contribution in case any amount the aggregate of which, in any financial year, exceed five per cent of its average net profits for the three immediately preceding financial years.
- (c) **In case of Political Party:** As per section 182(1), a company may contribute any amount directly or indirectly to any political party. However, no such contribution shall be made by a company unless a resolution authorising the making of such contribution is passed at a meeting of the Board of Directors and such resolution shall, subject to the other provisions of this section, be deemed to be justification in law for the making of the contribution authorised by it.

**(ii) Quantum of contribution**

- (a) **In case of National Defence Fund: As per section 183,** the Board of Directors

of any company or any person or authority exercising the powers of the Board of Directors of a company, or of the company in general meeting, may, notwithstanding anything contained in sections 180, 181 and 182 or any other provision of this Act or in the memorandum, articles or any other instrument relating to the company, contribute such amount as it thinks fit to the National Defence Fund or any other Fund approved by the Central Government for the purpose of national defence.

Hence, the company can contribute ₹ 7 Lakhs to National Defence Fund inspite of restriction by the company to contribute in any financial year for a sum not exceeding ₹ 5 lakhs as the Section 183 prevails over Articles of the company and there is no limit on such contribution.

- (b) **Bonafide Charitable Fund:** According to section 181, the Board of Directors of a company may contribute to *bona fide* charitable and other funds. However, prior permission of the company in general meeting shall be required for such contribution in case any amount the aggregate of which, in any financial year, exceed five per cent of its average net profits for the three immediately preceding financial years.

Average Net profit: ₹ 30 Lakhs  $[(45+25+20)/3]$

5% of average net profit: ₹ 1.5 Lakhs

Since, the amount of contribution exceeds five per cent of its average net profits for the three immediately preceding financial years, hence it requires prior permission of the company in general meeting for contributing ₹ 3 Lakhs to a bonafide Charitable Fund.

- (c) **Political party:** Section 182 specifies that a company other than a Government company and a company which has been in existence for less than three financial years, may contribute any amount directly or indirectly to any political party.

Hence, the company can contribute ₹ 5 Lakhs to a political party.

(iii) **Mode of payment of such contribution:**

- (a) **National Defence fund:** No mode of payment is provided under section 183.
- (b) **Bonafide Charitable Fund:** No mode of payment is provided under section 181.
- (c) **Political Party:** According to Section 182(3A), notwithstanding anything contained in sub-section (1), the contribution under this section shall not be made except by an account payee cheque drawn on a bank or an account payee bank draft or use of electronic clearing system through a bank account. However, a company may make contribution through any instrument, issued pursuant to any scheme notified under any law for the time being in force, for contribution to the political parties.

**Question 2**

(A) A group of shareholders of M/s. 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? **(4 Marks)**

(B) At the meeting of the members of M/s QRS Limited, a scheme of compromise and arrangement was approved by requisite majority. The National Company Law Tribunal (NCLT) after complying the provisions, issued an Order, approving the scheme of compromise and arrangement.

List out the matters to be provided in the Order issued by NCLT under Section 230(7) of the Companies Act, 2013.

When shall the Order be filed with ROC? **(4 Marks)**

(C) M/s. AWP Limited defaulted in repayment of a term loan taken from a Nationalized Bank against the security created as first charge on its Land & Buildings. The Bank classified the debt from M/s AWP Limited as Non-Performing Asset. The Bank issued Notice pursuant to Section 13 of the SARFAESI Act, 2002 to the Company to discharge its liabilities in full within a period of 60 days from the date of Notice. The Company objected for full settlement and the time limit for settlement. The Bank did not respond to the objection of the Company. In the light of the provisions of the SARFAESI Act, 2002 decide:

- (i) Whether the objection of the Company is valid?
- (ii) Whether the Bank has to respond to the objection of the Company?
- (iii) Whether the Bank has right to enforce the security interest without the intervention of the Court? **(6 Marks)**

**Answer**

- (A) (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).
- (B)** 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)]

- (C)** (i) As per section 13(2) of the SARFAESI Act, 2002, where any borrower, who is under a liability to a secured creditor under a security agreement, makes any default in repayment of secured debt or any instalment thereof, and his account in respect of such debt is classified by the secured creditor as non-performing asset, then, the secured creditor may require the borrower by notice in writing to discharge in full his liabilities to the secured creditor within sixty days from the date of notice failing which the secured creditor shall be entitled to exercise all or any of the rights under sub-section (4).

In the instant case, the bank issued notice to the company to discharge its liabilities in full within a period of 60 days from the date of notice and the company objected for

full settlement and the time limit for settlement. In view of the provisions of the section 13(2) mentioned above, the objection of the company is not valid.

- (ii) If, on receipt of the notice under sub-section (2), the company makes any representation or raises any objection, the bank shall consider such representation or objection and if the bank comes to the conclusion that such representation or objection is not acceptable or tenable, it shall communicate within fifteen days of receipt of such representation or objection the reasons for non-acceptance of the representation or objection to the company. [Section 3A]
- (iii) Notwithstanding anything contained in Section 69 or Section 69A of the Transfer of Property Act, 1882, the security interest created in favour of the bank may be enforced without intervention of the court or tribunal.

### Question 3

(A) *In the light of the provisions of the Companies Act, 2013, examine whether the following Companies can be considered as a 'Foreign Company':*

- (i) *M/s Red Stone Limited is a Company registered in Singapore. The Board of Directors meets and executes business decisions at their Board Meeting held in India.*
- (ii) *M/s Blue Star Public Company Limited registered in Thailand has authorized Mr. 'Y' in India to find customers and to enter contracts with them on behalf of the Company.*
- (iii) *M/s Xex Limited Liability Company registered in Dubai has installed its main server in Dubai for maintaining office automation software by Cloud Computing for its client in India.* **(8 Marks)**

(B) *Mr. 'B' purchased a flat out of the proceeds earned by Drug Trafficking. The flat was attached by the Director, Director of Enforcement after complying the procedures under Section 5 of the Prevention of Money Laundering Act, 2002 (PMLA, 2002). Mr 'B' got a stay from the High Court for any proceedings under the said Act. The stay was subsequently vacated.*

*State the relevant provisions of the PMLA, 2002 for computing the period of provisional attachment including extension, if any.*

*Whether Mr. 'C', son of Mr. 'B' can occupy the flat during the period of provisional attachment?* **(6 Marks)**

### Answer

- (A) According to section 2(42) of the Companies Act, 2013, "Foreign company" means any company or body corporate incorporated outside India which-
- (a) has a place of business in India whether by itself or through an agent, physically or through electronic mode; and
  - (b) conducts any business activity in India in any other manner.

According to the *Companies (Registration of Foreign Companies) Rules, 2014*, “**electronic mode**” means carrying out electronically based, whether main server is installed in India or not, including, but not limited to-

- (a) business to business and business to consumer transactions, data interchange and other digital supply transactions;
- (b) offering to accept deposits or inviting deposits or accepting deposits or subscriptions in securities, in India or from citizens of India;
- (c) financial settlements, web based marketing, advisory and transactional services, database services and products, supply chain management;
- (d) online services such as telemarketing, telecommuting, telemedicine, education and information research; and
- (e) all related data communication services,

whether conducted by e-mail, mobile devices, social media, cloud computing, document management, voice or data transmission or otherwise.

- (i) In the given situation, M/s Red Stone Limited is registered in Singapore. However, it does not have a place of business in India whether by itself or through an agent, physically or through electronic mode; and does not conduct any business activity in India in any other manner. Mere holding of board meetings and executing business decisions in India cannot be termed as conducting business activity in India. Hence, M/s Red Stone Limited is not a foreign company as per the Companies Act, 2013.
  - (ii) In the given situation, M/s Blue Star is registered in Thailand. It has authorised Mr. Y in India to find customers and enter into contract on behalf of the company. Thus, it can be said that M/s Blue Star Limited has both place of business in India through an agent, physically or through electronic mode; and is conducting business activity in India. Hence, M/s Blue Star Limited is a foreign company as per the Companies Act, 2013.
  - (iii) In the given situation, M/s Xex Limited Liability Company is registered in Dubai and has installed its main server in Dubai for maintaining office automation software by Cloud Computing for its client in India. Thus, it can be said that M/s Xex Limited Liability Company has a place of business in India through electronic mode and is conducting business activity in India. Hence, M/s Xex Limited Liability Company is a foreign company as per the Companies Act, 2013.
- (B) According to section 5 of the Prevention of Money Laundering Act, 2002, where the Director or any other officer (not below the rank of Deputy Director authorised by the Director), has reason to believe (the reason for such belief to be recorded in writing), on the basis of material in his possession, that—
- (a) any person is in possession of any proceeds of crime; and



- (b) such proceeds of crime are likely to be concealed, transferred or dealt with in any manner which may result in frustrating any proceedings relating to confiscation of such proceeds of crime under this Chapter,

he may, by order in writing, provisionally attach such property for a period not exceeding 180 days from the date of the order, in such manner as may be prescribed.

Provided further that, any property of any person may be attached under this section if the Director or any other officer not below the rank of Deputy Director authorised by him has reason to believe (the reasons for such belief to be recorded in writing), on the basis of material in his possession, that if such property involved in money-laundering is not attached immediately under this Chapter, the non-attachment of the property is likely to frustrate any proceeding under this Act.

**Computation of period of attachment:** Provided also that for the purposes of computing the period of 180 days, the period during which the proceedings under this section is stayed by the High Court, shall be excluded and a further period not exceeding 30 days from the date of order of vacation of such stay order shall be counted.

**No effect on the right to enjoy the property:** This section shall not prevent the person interested in the enjoyment of the immovable property attached from such enjoyment.

Here, “**person interested**”, in relation to any immovable property, includes all persons claiming or entitled to claim any interest in the property.

In the given case, Mr. C, son of Mr. B can occupy the flat during the period of provisional attachment if he claims to have any interest in the said property.

#### Question 4

- (A) 'X' Stock Exchange Limited was granted recognition by Securities and Exchange Board of India (SEBI). The stock brokers of the Stock Exchange did not pay much heed to the concept of governance and focused on increasing their wealth and snubbed the protection of investors. Their activities were against the interest of the trade and general public.
- (i) Examine whether the Central Government / SEBI has the power to withdraw the recognition granted to 'X' Stock Exchange Limited under the provisions of Securities Contracts (Regulations) Act, 1956?
- (ii) Whether a person can be a member of an unrecognized Stock Exchange for the purpose of performing any contracts in Securities? **(4 Marks)**
- (B) 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?* **(4 Marks)**

(C) *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 & C; 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 ₹ 25,000.* **(6 Marks)**

**Answer**

(A) (i) Section 5(1) of the Securities Contracts (Regulations) Act, 1956 states that if the Central Government/ SEBI is of the opinion that the recognition granted to a stock exchange under the provisions of this Act, should, in the interest of the trade or in the public interest, be withdrawn, the Central Government or SEBI may serve on the governing body of the stock exchange, a written notice that the Central Government or SEBI is considering the withdrawal of the recognition for the reasons stated in the notice and after giving an opportunity to the governing body to be heard in the matter, the Central Government/SEBI may withdraw the recognition granted to the stock exchange.

Thus, Central Government/ SEBI can withdraw the recognition of 'X' Stock Exchange Limited on the grounds that their activities were against the interest of the trade and general public.

(ii) As per section 19 of the Securities Contracts (Regulations) Act, 1956, no person shall organise or assist in organising or be a member of any stock exchange (other than a recognised stock exchange) for the purpose of assisting in, entering into or performing any contracts in securities, except with the approval of Central Government or SEBI.

Hence, no person can be a member of an unrecognised Stock exchange for the purpose of performing any contracts in Securities, except with the approval of Central Government or SEBI.

(B) **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) 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.

- (C) (i) As per section 2(j) of the FCRA, 2010, "foreign source" includes a society, club or other association or individuals formed or registered outside India. Accordingly in the given case, amount (i.e., loan) received by M/s KG & Co., being a partnership firm not covered under the above provisions, from club registered in London for its business purpose, is permissible.
- (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 fund 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 ₹ 25,000/- currently).

In the given situation, Mr. Happy received the wrist watch (market value ₹ 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.

#### Question 5

- (A) *Due to an unprecedented flood, all the fixed assets of a Company were damaged extensively beyond renovation or repair. The cost 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 to the winding-up petition and also filed an appeal against the winding-up order. The workers are 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? (4 Marks)*
- (B) *M/s KIL Limited, a listed company, proposed to acquire a plant for consideration other than cash from Mr. KK, a director. The Managing Director of the Company identified Mr. JK a registered valuer under the provisions of the Companies Act, 2013 for the purpose of valuation of the plant. Mr. KK acquired the plant 48 months back from a partnership firm in which the spouse of Mr. JK is a partner. The Managing Director of the Company issued an order appointing Mr. JK as a registered valuer. Examine and decide whether the decision of appointment and the mode of appointment is valid under the provisions of the Companies Act, 2013? (4 Marks)*
- (C) *In view of the deep recession prevailing in, the market for the past three years, M/s. Infra Limited (Corporate Debtor), which was facing the brunt of financial crisis, could not pay salaries and wages to its workmen and employees for the past 6 months. The workmen and the employees, who are the members of a recognized Trade Union "Infra Labor Federation", made a complaint in this regard. Thereafter, the Trade Union approached and urged the Management of the Company in person and through representations in writing to settle the arrears of wages and salaries due to its members. The Corporate Debtor neither disputed nor took any actions to settle the amount. Under the circumstances, Infra Labor Federation filed an application before the Adjudicating Authority i.e. with the National Company Law Tribunal for initiating a Corporate Insolvency Resolution Process under the Insolvency and Bankruptcy Code, 2016.*

*In the light of the provisions of the Insolvency and Bankruptcy Code, 2016, examine the following:*

- (i) *Validity of the Application.*
- (ii) *What will be the "Initiation date" for initiating the Corporate Insolvency Resolution Process? (6 Marks)*

**Answer**

- (A) 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 question, 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.

- (B) 1. **Restriction on acquiring assets for consideration other than cash:** According to Section 192 (1) of the Companies Act, 2013, 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.
2. **Relaxation of restriction:** The above restriction shall be relaxed i.e. the company may enter into an arrangement involving non-cash transactions, if prior approval for such arrangement is accorded by a resolution of the company in general meeting.
3. **Contents of notice issued for approval of resolution:** The notice for approval of the resolution in general meeting issued by the 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.
4. As per section 247(2) of the Companies Act, 2013, the valuer shall 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 3 years prior to his appointment as valuer or 3 years after the valuation of assets was conducted by him.

As per the facts of the question and the provisions of the Act, M/s KIL Limited acquired plant from consideration other than cash from Mr. KK, a director. The Act has restricted such a non-cash transaction from a director. The company can enter into such a transaction only if it obtains prior approval for the same in general meeting. It is also required that notice for such meeting shall also include the value of the assets involved in such arrangement duly calculated by a registered valuer.

As per further facts of the question, the Managing director of the company identified Mr. JK to be the registered valuer. Mr. KK acquired the plant 48 months (i.e. 4 years) back from a partnership firm in which the spouse of Mr. JK is a partner.

In the light of the facts of the question and provision of law, since more than 3 years (here 4 years) has passed when Mr. KK acquired the asset from a partnership firm in which the spouse of Mr. JK is a partner, Mr. JK can be validly appointed as a registered valuer.

However, according to section 247(1) of the Companies Act, 2013, where a valuation is required to be made in respect of any property, it shall be valued by a person having such qualification 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.

In view of above, the mode of appointment of Mr. JK is not valid as he is appointed by the Managing Director of the company.

- (C) **Workmen & Employees as Operational Creditor:** The Insolvency and Bankruptcy Code, 2016 considers all employees and workmen as operational creditors.

As per section 5(20) of the Code, "*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;"

Whereas 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 repayment 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."

Accordingly, if there is any dues arising in the course of employment, then that will be considered as an operational debt and the person to whom such operational debt is owed shall be treated as the Operational Creditor. Therefore, workmen & employees shall be treated as Operational Creditor of the Corporate Debtor.

The term "person" as defined under section 3(23) of the IBC, 2016 includes "any other entity established under any statute". A trade union, when registered under the Trade Union Act, 1926 would come within the purview of any other entity "established" under the statute.

**Filing of an application by Operational Creditor:** Application can be filed by the Operational Creditor in the NCLT if there is a debt, in compliance with sections 8 & 9 of the Code.

Prior to filling the application before NCLT, an employee has to comply with the procedure of sending the demand notice to the Corporate Debtor. If the Corporate Debtor has not paid the amount of debt even after sending the demand notice, neither intimated to the operational creditor about the existence of any regarding the dispute pertaining to the due debts.

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 date of filing of the application before the NCLT will be the initiation date for initiating the Corporate Insolvency Resolution Process (Section 5(11)).

Accordingly, in the light of the given provisions, following are the answers:

- (i) Application filed by trade union, Infra Labor Federation on behalf of the workmen & employees in the said instance is valid as operational debt had been being legally assigned to the trade union in terms of section 5(20) of the Code and is included in the definition in section 3(23) of IBC, 2016.
- (ii) Trade union, Infra Labour Federation may file an application before the Adjudicating Authority for initiating a corporate insolvency resolution process after expiry of 10 days from the date of serving demand notice to the M/s Infra Ltd and the date of filing of the application before the NCLT will be the date of initiation.

#### Question 6

(A) *Mr. 'K' is a small shareholder director in M/s KGP Tyres Limited from 1st April 2018 and in M/s VSR Cotton Mills Limited from 1st April 2019, in compliance with the relevant provisions of the Companies Act, 2013. M/s KGP Tyres Limited has not paid interest on the public deposits due from 1st July 2018. In the light of the information given above, examine the following under the provisions of the Companies Act, 2013.*

- (i) *Whether the office of Mr. 'K', small shareholder director, shall become vacant in M/s KGP Tyres Limited and M/s VSR Cotton Mills Limited?*
- (ii) *If yes, state the period from which the office of the directorship shall become vacant.*

**(4 Marks)**

OR

*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? (4 Marks)*
- (B) *Mr. Thangavel is a Director in 7 Companies with a DIN (Director Identification Number) allotted to him. Again, another DIN was inadvertently allotted to him which was never used for filing any document with any Authority. He desires to surrender the second DIN and keep all his directorship with the first DIN. Advise him the procedure to be followed under the provisions of the Companies Act, 2013 and the Rules made thereunder for surrendering the second DIN inadvertently obtained by him. (4 Marks)*
- (C) *Mr. 'K' used his car for smuggling cash and the Special Court found on conclusion of trial that an offence of money laundering was committed by Mr. 'K' under the provisions of the Prevention of Money Laundering Act, 2002 (PMLA, 2002). The car was under hypothecation to a Nationalized Bank for the car loan obtained. Referring to provisions of the PMLA, 2002, examine whether the car can be confiscated despite the existence of encumbrance? (3 Marks)*
- (D) *The Committee of Creditors of M/s XYZ Limited proposes to appoint Mr. Ajit, an Insolvency Professional, as Insolvency Resolution Professional in the matter of corporate insolvency process of M/s XYZ Limited. Mr. Ajit was a promoter of M/s ABC Limited which is a holding company of M/s XYZ Limited. Examine and decide whether Mr. Ajit is eligible for appointment as an Insolvency Resolution Professional under the Provisions of Insolvency and Bankruptcy Code, 2016. (3 Marks)*

#### **Answer**

- (A) According to Rule - 7, *Companies (Appointment and Qualification of Directors) Rules, 2014*, a person shall not be appointed as small shareholders' director of a company, if the person is not eligible for appointment in terms of section 164.

Also, a person appointed as small shareholders' director shall vacate the office if the director incurs any of the disqualifications specified in section 164.

According to Section 167(1)(a), the office of a director shall become vacant in case he incurs any of the disqualification specified in section 164. Provided that when he incurs disqualification under section 164(2), the office of the director shall become vacant in all companies, other than the company which is in default under that sub section [inserted by Companies (Amendment) Act, 2017 w.e.f. 07-05-2018]

According to proviso of section 164(2) of the Companies Act, 2013, where a person is appointed as a director of a company which is in default of clause (a) or clause (b), he shall



not incur the disqualification for a period of six months from the date of his appointment.

In the instant case, M/s KGP Tyres Limited has not paid interest on the public deposits due from 1<sup>st</sup> July, 2018 and disqualification under section 164(2)(b) of the Companies Act, 2013 occurs on a person who is or has been a director of a company which has failed to repay the deposits accepted by it or pay interest thereon and such failure to pay or redeem continues for one year or more. Accordingly, following are the answers:

- (i) Yes, the office of Mr. K shall become vacant in M/s VSR Cotton Mills Limited as he has become disqualified under section 164(2)(b) from 1<sup>st</sup> July 2019 but not in M/s KGP Tyres Limited.
- (ii) Mr. K's office of the directorship shall become vacant from 1<sup>st</sup> July, 2019.

**OR**

- (A) (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.

- (B) **According to Rule 11 of the Companies (Appointment and Qualification of Directors) Rules, 2014:** 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 fee as specified from any person, cancel or deactivate the DIN in case on an application made in Form DIR-5 by the DIN holder to surrender his DIN along with declaration that the said DIN has never been used for filing of any document with any authority, the Central Government may deactivate such DIN.

Provided that before deactivation of any DIN in such case, the Central Government shall verify e-records.

- (C) **Vesting of property in Central Government [Section 9]:** Where an order of confiscation has been made under section 8(5) or section 8(7) or section 58B or section 60(2A) of PMLA, 2002 in respect of any property of a person, all the rights and title in such property shall vest absolutely in the Central Government free from all encumbrances.

However, where the Special Court or the Adjudicating Authority, as the case may be, after giving an opportunity of being heard to any other person interested in the property attached under this Chapter, or seized or frozen, is of the opinion that any encumbrance on the property or lease-hold interest has been created with a view to defeat the provisions of this Chapter, it may, by order, declare such encumbrance or lease-hold interest to be void and thereupon the aforesaid property shall vest in the Central Government free from such encumbrances or lease-hold interest.

In the instant case, Mr. K used his car for smuggling cash and Special Court found on conclusion of trial that an offence of money laundering was committed by Mr. K. The car was under hypothecation to a Nationalized bank for the car loan obtained. As the encumbrance on the car has been created to defeat the provisions and special court may order to declare such encumbrance to be void and therefore the car can be confiscated and shall vest in the Central Government.

- (D) 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 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.

In the given instance, Committee of Creditors of M/s XYZ Ltd. proposed to appoint Mr. Ajit, as IRP in the matter of corporate insolvency resolution process of M/s XYZ Ltd. However, Mr. Ajit was a promoter of M/s ABC Ltd. which is a holding company of M/s XYZ Ltd.

Accordingly, Mr. Ajit, is a related party of the corporate debtor. Therefore, Mr. Ajit is not eligible for appointment as an insolvency resolution professional in terms of the said legal provisions of the Code.