CHAPTER 2

MEETINGS OF BOARD AND ITS POWERS.

CONTENTS OF THE CHAPTER:

- The procedure and requirements of convening the Board meeting.
- The requisite quorum for the conduct of the meeting.
- The Audit committee, Nomination and Remuneration Committee and Stake holders Relationship Committee of the Board.
- The powers and restriction on powers of Board.
- The various provisions related to contribution of companies to charitable funds, towards political contributions, National defence fund, etc.
- Provisions related to additional director, alternate director, nominee director and casual vacancy.
- Provisions related to disclosure of interest by directors, restrictions on Loan to directors and loans and investments made by company.
- The concept related to related party and related party transactions.
- The provisions in relation to payment to director for loss of office, etc., restrictions on non-cash transactions with directors, Prohibition on forward dealings in securities by director /KMP, and prohibition on insider trading of securities.
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INTRODUCTION:
Two main organs, the shareholders in general meetings and the directors acting as a Board conduct the affairs of a company. Therefore, directors frequently meet up to discuss various matters relating to the management and administration of the affairs of the company in the interest of the public and the shareholders. The modern practice is to confer upon the directors the right to exercise all company’s powers except for those matters, which are by law required to be exercised by the company in general meeting. The Board of directors oversees management of the company to ensure that the interests of shareholders are protected.

The provisions related to meetings of Board and its powers are dealt under sections 173 to 195 of the Companies Act, 2013 and Rules. This chapter specifies the laws related to convening of Board meeting, requisite quorum for the conduct of the meeting, various committees of the Board, Powers of Board and the imposed restrictions, Disclosure of interest by directors, Loan and investment, related party transactions and etc.

SECTION 173 : MEETINGS OF BOARD.

1. FREQUENCY OF BOARD MEETING:
   a) First Board Meeting: Every company shall hold the first meeting of the Board of Directors within thirty days of the date of its incorporation.
   b) Subsequent Board Meeting: Every company shall hold a
      ➔ Minimum 4 meetings of its Board of Directors every year
      AND
      ➔ provided that Maximum gap between two consecutive Board Meetings should not be more than 120 days.

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.

c) Central Government may, by notification, exempt any class of companies form section 173

In case of Specified IFSC Public Company and IFSC Private Company - In sub-section (1) of Section 173, after the proviso, the following proviso shall be inserted, namely:-
“Provided further that a Specified IFSC public company shall hold the first meeting of the Board of Directors within sixty days of its incorporation and thereafter hold at least one meeting of the Board of Directors in each half of a calendar year.”. Notification Dated 4th January 2017.

Vide Notification G.S.R. 466(E) dated 5th June 2015, this sub-section 1 of section 173 shall apply to the company formed under section 8 of the Companies Act, 2013 only to the extent that the Board
of Directors, of such companies shall hold at least one meeting within every six calendar months.

**Question 1.**
The Board of directors of ABC Ltd. met thrice in the year 2014 and the 4th Meeting, though called, could not be held for want of quorum.
Examine with reference to the relevant provisions of the Companies Act, 2013, Whether any provisions of the Companies Act, 2013 have been contravened?

**Answer**
In terms of section 173(1) of the Companies Act, 2013, a company must hold a minimum number of four meetings every year of its Board of directors in such a manner that not more than 120 days shall intervene between two consecutive meetings of the Board.

Further, the proviso to this subsection provides that the Central Government may by notification, direct that these provisions will not apply in relation to any class or description of companies or may apply subject to such exceptions, modifications or conditions as may be specified in the notification.

Under section 174 (4) of the Companies Act, 2013 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.

From the above provisions in case a meeting is adjourned, the violation under section 173(1) does not arise as the meeting was started well in time but could not close due to want of quorum. The holding of the adjourned meeting though in the next year will be treated as continuation of the 4th meeting of the previous year and will therefore not count in the meetings held in the next year but in the previous year.

Therefore, the provisions of the Companies Act, 2013 have not been violated or contravened.

2. **PARTICIPATION IN BOARD MEETING:**
   a) The participation of directors in a meeting of the Board may be
      ➔ either in person or
      ➔ through video conferencing or
      ➔ other audio visual means as may be prescribed under Rule 3 of the Companies (Meetings of Board and its Powers) Rules, 2014.

   b) Such other audio visual capable of recording and recognising the participation of the directors and storing the proceedings of such meetings along with date and time.

   c) However, the Central Government may by notification specify such matters as given under Rule 4 of the Companies (Meetings of Board and its powers) Rules, 2014 which shall not be dealt with in a meeting through video conferencing and other audio visual means.

   “Video conferencing or other audio visual” 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.
As per Rule 4, the following matters shall not be dealt with in any meeting held through video conferencing or other audio visual means.-

i. The approval of the annual financial statements;
ii. The approval of the Board’s report;
iii. The approval of the prospectus;
iv. The Audit Committee Meetings for consideration of financial statement including consolidated financial statement if any, to be approved by the board under sub- section (1) of section 134 of the Act, and
v. The approval of the matter relating to amalgamation, merger, demerger, acquisition and takeover.

d) It is provided 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 those matters also which are not permitted to be dealt with in a meeting through video conferencing or other audio visual means. These matters are enumerated above.

e) Some of the key points related to meetings of Board that are held through conferencing or other audio visual means, as provided in Rule 3 of the Companies (Meetings of Board and its Powers) Rules, 2014 are as under:

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<th>Sr. No.</th>
<th>Key points related to meetings of Board that are held through conferencing or other audio visual means.</th>
<th>For convening and conducting the Board meetings</th>
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<td>1.</td>
<td>Every Company shall make necessary arrangements</td>
<td>(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...</td>
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<td>2.</td>
<td>The Chairperson of the meeting and the company secretary, if any, shall take due and reasonable care-</td>
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| 3. | Notices of the meeting and the further process | (A) shall be sent to all the directors in accordance with the provisions of Section 173 (3)  
(B) shall inform the directors regarding the options available to them to participate through video conferencing mode or other audio visual means, along with all other 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 chairman 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 arrangements in this behalf.  
(E) The director, who desires, to participate may intimate his intention of participation through the electronic mode at the beginning of the calendar year and such declaration shall be valid for one calendar year.  
(F) In the absence of any such intimation from the director, it shall be assumed that he will attend the meeting in person. |
| 4. | Process of a roll call at the Board Meeting | A director participating in a meeting through video conferencing or other audio visual means shall be counted for the purpose of quorum, unless he is to be excluded for any items of business under any provisions of the Act or the rules. |
| 5. | Scheduled venue of the meeting as mentioned in the notice convening the meeting | 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. |
| 6. | Circulation of draft minutes of the | among all the directors within 15 days of the |
Chap. 2. Meetings of Board and its Powers.

<table>
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<th>meeting</th>
<th>meeting either in writing or in electronic mode as may be decided by the Board.</th>
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<td>7.</td>
<td>After completion of meeting Minutes shall be entered in the minute book signed by the chairperson</td>
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3. **NOTICE OF BOARD MEETING:**
   - a) Notice to: every director;
   - b) Address: at his registered address
   - c) Whether in or outside India: Both
   - d) Length: **Atleast seven days** before the meeting.
   - e) Modes: MUST BE IN WRITING. Sent by post or by electronic means or by hand delivery.
   - f) Shorter notice --- Valid. Subject to following 2 conditions.
     - i) To transact urgent business
     - AND
     - ii) At least one independent director, if any, must be present at the meeting:
   - g) In case of absence of independent directors from such a Board meeting (called by shorter notice), decisions taken at such a meeting shall be final subject to following 2 conditions:
     - i) decisions taken must be circulated to **ALL** the directors
     - AND
     - ii) Must be ratified by atleast by at least 1 independent director, if any.
   - h) Notice must specify availability of option for the directors to participate through video conferencing.

**Question 2**

*What are the conditions to be fulfilled for calling meetings at shorter notice than as prescribed by Companies Act, 2013.*

*One of the directors, a senior professional, objected to receiving the notice by e-mail. Advise him.*

**Answer**

*Notice of The Board Meeting and Condition to Call Meeting at Shorter Notice - 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.

Under Section 173 (3) a meeting of the Board shall be called by giving not less than 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.

Hence the senior Director’s objections to receiving the notice by email is not sustainable.*

4. **FAILURE TO GIVE NOTICE:**
   Every officer in default shall be liable to a penalty of **twenty-five thousand** rupees.*

   *According to Secretarial Standard 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 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.

5. **EXCEPTION**: One Person Company, small company and dormant company and a private company (if such private company is a start-up) (#Amendment):

   a) Sec 173(1) does not apply to One Person Company, small company and dormant company and a private company (if such private company is a start-up).

   As per section 173(5), section 173 is deemed to be complied with for such companies if:

   i) It conducts at least one Board meeting in each half of a calendar year  
      AND
   ii) The gap between the two meetings is MINIMUM 90 days

   b) Provided that One Person Company in which there is only one director on its Board of Directors, need not comply with the requirements mentioned in (a) above. Thus it is exempt from Section 173(5).

   c) 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.

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**Question 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 whom should the notice of Board meeting be given to the “original director” or to the “alternate director”?

**Answer**

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, 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 a 7 days’ notice in writing to every director to his registered address 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 matter of prudence the notice of the meeting may be served to both the alternate director as well as the original director who is for the time being outside India.

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2.8
Question 4.
The Board of Directors of M/s Infotech Consultants Limited, registered in Calcutta, proposes to hold the next board meeting in the month of May, 2014. They seek your advice in respect of the following matters:
(i) Can the board meeting be held in Chennai, when all the directors of the company reside at Calcutta?
(ii) Is it necessary that the notice of the board meeting should specify the nature of business to be transacted?
Advise with reference to the relevant provisions of the Companies Act, 2013

Answer
(i) There is no provision in the Companies Act, 2013 under which the board meetings must be held at any particular place. Therefore, there is no difficulty in holding the board meeting at Chennai even if all the directors of the company reside at Calcutta and the registered office is situated at Calcutta provided that the requirements regarding the holding of a valid board meeting, etc. are complied with.
(ii) Section 173(3) of the Companies Act, 2013 provides for the giving of notice of every board meeting of not less than seven days to every director of the company. There is no provision in the Act laying down the contents of the notice. Hence, it may be construed that notice may be interpreted as intimation of the meeting and does not necessarily include the sending of the Agenda of the meeting. However, as a matter of good secretarial practice, the notice should include full details and particulars of the business to be transacted at the Board Meetings.
The articles of association of the company may make it mandatory to do so in almost all cases.

Question 5.
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. State in this connection whether such a provision in the Articles of Association of a foreign collaborated company is valid within the purview of the provisions of the Companies Act, 2013.

Answer
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 clear that the notice shall be sent by hand delivery or by post or by electronic means.
Hence, the sending of notice by e-mail is an ordinary mode of sending notice of a board meeting under the Companies Act, 2013.

Therefore, in the given case the shorter notice is legally permitted with the only condition being the presence of the quorum and at least one independent director. The provision of the Articles in this regard is not relevant as the position is amply clarified in the Act itself.

Question 6.
1. State the legal requirements to be complied with by a public company in respect of a Board Meeting.

2. 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).

**Answer**

1. Legal requirements to be complied with by a public company in respect of a Board Meeting:
   (a) **Frequency of meeting:** Section 173(1) -- first Board meeting within 30 days. -- Subsequent meetings, at least four in a year -- not more than one hundred and twenty days gap between two board meetings.
   (b) **Notice of meeting:** Section 173(3) -- not less than 7 days’ notice in writing to every director at his address registered with the company -- sent by hand delivery or by post or by electronic means. Further, a meeting may be called at shorter notice -- urgent business AND at least one independent director attends, if any.
   (c) **Quorum for meetings:** Section 174(1), the quorum for a meeting -- one-third of its total strength, or two directors, whichever is higher -- The directors participating by video conferencing or any other audio visual means shall be counted for the purposes of determining the quorum.
   (d) **Adjourned meeting:** According to Section 174(4) of the Act, if a meeting of the Board could not be held for want of quorum, then, unless the articles otherwise provide, the meeting shall automatically stand adjourned till the same day in the next week, at the same time and place, or if that day is a national holiday, till the next succeeding day which is not a national holiday, at the same time and place.

2. Notice of Board meeting

   (i) **An Interested Director:** Section 173(3) of the Companies Act, 2013 makes it mandatory for every director 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 a director even though he is precluded from voting at the meeting on the business to be transacted

   (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

   (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. This is important because the Companies Act, 2013 permits a director to participate in a meeting by video conferencing or any other audio visual means.
SECTION 174 : QUORUM FOR BOARD MEETING.

A quorum is the minimum number of qualified persons who must attend in order to transact business at a duly convened Board meeting. A meeting shall not be deemed to have been properly held unless the quorum was present at that meeting.

Section 174 of the Companies Act, 2013 provides for Quorum for meetings of Board. According to this section:

1. The quorum for a meeting of the Board of Directors of a company is one third of its total strength or two directors, whichever is higher, and the participation of the directors by video conferencing or by other audio visual means shall also be counted for the purposes of quorum under this sub-section.

Further, the explanation as given in Rule 3 of the Companies (Meetings of Board and its Powers) Rules, 2014 provides that the director participating in a meeting through video conferencing or other audio visual means shall be counted for the purpose of quorum, unless he is to be excluded for any items of business under any provisions of the Act or the rules.

2. Vide Notification G.S.R.466(E) dated 5th June 2015 the companies covered under section 8 of the Companies Act, 2013 shall constitute quorum for the Board meeting, either eight members or 25% of its total strength whichever is less. Provided that quorum shall not be less than two members.

*Section 8 companies: Quorum = 8 members or 25% of total strength (minimum 2).

3. The continuing directors may notwithstanding any vacancy in the Board; but, if and so long as their number is reduced below the quorum fixed by the Act for a meeting of the Board, the continuing directors or director may act for the purpose of increasing the number of directors to that fixed for the quorum, or of summoning a general meeting of the company and for no other purpose.

4. If at any time the number of “Interested Directors” is more than or equal to two thirds of the total strength of the Board of Directors, The quorum will be: Remaining number of directors being disinterested, present at the meeting, being not less than two. {i.e. Min 2 disinterested directors must be present in such a case}

“Interested director” for the purposes of this sub section means a director within the meaning of section 184 (2).
Exemptions:

In case of Specified IFSC Public Company and IFSC Private Company - Section 174(3) shall apply with the exception that interested director may participate in such meeting provided the disclosure of his interest is made by the concerned director either prior or at the meeting. - Notification Dated 4th January, 2017.

Vide Notification No. G.S.R. 464(E) dated 5th June 2015, this Sub section (2) of section 184 shall apply on private company with the exception that the interested director may participate in such meeting after disclosure of his interest.

Notes:
1. For the purpose of calculating quorum, any fraction of a number shall be rounded off as one.
2. “Total strength” shall not include directors whose places are vacant.

5. Where quorum is not present, then, the meeting shall automatically stand adjourned.
6. Provided that One Person Company in which there is only one director on its Board of Directors, is exempt from provisions of Section 174.

Question 7.
(i) What is the procedure to be followed, when a board meeting is adjourned for want of quorum?

Answer
(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.

It may be noted that on adjournment of a meeting, the meeting having started and not ended will not constitute a contravention of section 173(1) under which a company is required to hold four board meetings in a year and not more than 120 days shall elapse between two board meetings. In case of adjournment of the meeting, it shall be deemed to have been held on the date on which it was started and not on the date when the adjourned meeting was held.

Question 8.
1. PQR Limited held three board meetings till 31st October, 2014 during the financial year 2014. The next board meeting was due to be held on 27th December, 2014 but for want of quorum the meeting could not be held. A group of shareholders complained that the Company has violated the provisions of section 173 of the Companies Act, 2013 in not holding the required number of board meetings.
Further, Mr. P and Mr. Q who are the directors of the Company informed the Company their inability to attend the meeting because the notice of the meeting was not served on them. Discuss whether there is any default on the part of the Company and the consequences thereof. What will be the quorum in the given situation?

Answer

1. In terms of section 173(1) of the Companies Act, 2013, a company must hold a minimum number of four meetings of its Board of directors in such a manner that not more than 120 days shall intervene between two consecutive meetings of the Board.

Further, the proviso to this subsection provides that the Central Government may by notification, direct that these provisions will not apply in relation to any class or description of companies or may apply subject to such exceptions, modifications or conditions as may be specified in the notification.

Further, as per section 174(4) of the Act, if a meeting of the Board could not be held for want of quorum, then, unless the articles otherwise provide, the meeting shall automatically stand adjourned till the same day in the next week, at the same time and place, or if that day is a national holiday, till the next succeeding day which is not a national holiday, at the same time and place.

It may be noted that on adjournment of a meeting, the meeting having started and not ended will not constitute a contravention of section 173(1) under which a company is required to hold four board meetings in a year and not more than one hundred and twenty days shall elapse between two board meetings. In case of adjournment of the meeting, it shall be deemed to have been held on the date on which it was started and not on the date when the adjourned meeting was held.

Therefore, the provisions of section 173 shall not be deemed to have been contravened merely by reason of the fact that a meeting of the Board which had been called in compliance with the terms of that Section could not be held for want of a quorum.

As the meeting could not be held for want of quorum, it cannot be said that PQRLtd has violated the provisions of section 173 of the Act.

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 Rs. 25,000.

In the given case as no notice, was served on Mr. P and Mr. Q who are the directors of the company, thus, under section 173(4) every officer of the company responsible for the default shall be punishable with fine of Rs. 25,000.

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 as stipulated in the Act. We shall have to go by the provisions of the Act which clearly provide for the notice to be sent to every director failing which the resolutions passed will be invalid. 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. Notice must be given to each director in writing. Hence, even though the directors concerned knew about the meeting, the meeting shall not be valid and resolutions passed at the meeting also shall not be valid.
Question 9.
ABC Ltd. has 12 directors on its Board and has the following clause in its Articles of Association:
“The questions arising at any meeting of the Board of directors or any Committee thereof shall be decided by a majority of votes, except in cases where the Companies Act, 2013 expressly provides otherwise.”
In one of the meetings of the Board of directors of ABC Ltd., 8 directors were present. After completion of discussion on a matter, voting was done. 3 directors voted in favour of the motion, 2 directors voted against the motion while 3 directors abstained from voting.
You are required to state with reference to the provisions of the Companies Act, 2013 whether the motion was carried or not. It is clarified that the motion being voted upon was not concerning a matter which requires consent of all the directors present in the meeting.

Answer
Regulation 68 of Table F of Schedule 1 to the Companies Act, 2013 provides that save as otherwise expressly provided in the Companies Act, 2013, questions arising at any meeting of the Board shall be decided by a majority of votes.
In the problem given in the question, the similar article exists in the Articles of Association of ABC Ltd. In the given case, only 8 directors out of a total strength of 12 directors are present and out of those 8 directors present only 5 directors have exercised their votes. In such a case, only those directors who are present and vote on a motion are considered for determining whether the motion is carried or not. That means out of the 5 directors who voted on the motion are to be considered. Directors who did not vote will not be counted as either having voted in favour or against. Their votes will be disregarded. Accordingly, since number of directors who voted in favour of the motion being 3, is higher than the number of directors who voted against the motion being 2, the motion is carried or is considered to be passed by majority.

Question 10.
Analyse and Advise with reference to the provisions of the Companies Act, 2013, the following situations.
(a) There are 9 directors in a company and out of which 2 offices of the directors have fallen vacant. What will be the quorum for the Board Meeting?
(b) There are 15 directors in a company and during discussion of a particular item, 13 of the directors are said to be ‘interested’ within the meaning of section 184(2) of the Companies Act, 2013. What shall be quorum of the meeting?

Answer
(a) 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 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, we find: 1/3 of (9-2) = 1/3 of 7 = 2 1/3 directors which will be rounded off as 3. Being higher than 2, therefore 3 directors would constitute the quorum for the Board meetings.
(b) Under section 174(3) of the Companies Act, 2013 if at any time the number of the remaining directors exceeds or is equal to two thirds of the total strength of the Board of Directors, the number of the remaining directors who are non-interested but present at the meeting, not being less than two shall constitute the quorum. Accordingly in the given problem, there are in all 15 directors and the Board meeting commences...
with all the 15 directors. During the meeting, an item comes up for discussion in respect of which 13 happen to be “interested” directors. In this case, in spite of the excess of the interested directors being more than two-thirds, the prescribed minimum number of non-interested directors constituting the quorum, namely, 2 are present at the meeting and can transact the particular item of business.

**Question 11.**
A meeting of the Board of ‘No Holiday Ltd’ was held on a national holiday. However due to lack of quorum, the proceedings of the meeting could not be held and therefore the Chairman of the meeting decided with the consent of the majority that the Board meeting be adjourned to next Monday. However, the date fixed for the adjourned meeting happened to be a ‘national holiday’. Advise and draw your analogy with reference to the provisions of the Companies Act, 2013, whether the adjourned meeting of the Board can be held on a day which is a public holiday.

**Answer**
The Companies Act 2013 vide section 173(3) merely states that 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. It further provides for the board meeting to be held on shorter notice to transact urgent business subject to the condition that at least one independent director, if any, shall be present at the meeting. Therefore, as far as the holding of a board meeting is concerned, it may be held at any place on any day including a national holiday if agreed by the directors. However, when 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. Therefore, the adjourned meeting cannot be held on a national holiday unless the Articles of the company provide that it can. The meeting will have to be held on the next working day to the national holiday.

**Question 12.**
Examine, with reference to the relevant provisions of the Companies Act, 2013, the validity/legality of the following:
A meeting of the Board of directors of OPQ Co. Ltd. due to be held on 30.9.2014 did not take place for want of quorum. As a result, the Company did not hold any Board meeting for the quarter ended 30.9.2014 and there is a complaint that the Company has violated the provisions of the Act in this regard.

**Answer**
Section 173(1) of the Companies Act, 2013 requires a company to hold at least 4 board meetings in a year in such a manner that not more than 120 days shall elapse between two board meetings. Moreover, under section 174(4) in case a meeting is held but could not be continued due to want of quorum, the meeting gets adjourned to the same time and place next week and if such date is a national holiday to the next working day.
From the above therefore, there is no violation as the meeting was held on 30th Sept 2014 and the meeting will automatically be 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. Moreover, it is not necessary under the Companies Act, 2013 for a company to hold board meetings on quarterly basis as long as 4 meetings are held in a year. So considering the dates when other meetings were held, it may emerge that the company has not violated the provisions of the Companies Act, 2013. Thus, the allegation that the company has contravened the provisions of section 173(1) in the matter of holding the Board meeting is not correct.

SECTION 175 : RESOLUTION BY CIRCULATION.

1. Resolution by circulation:

   a) Passed by → The Board
   b) Procedure → The resolution is circulated in draft, together with the necessary papers, if any
   c) Circulated to → All the directors, at their addresses registered with the company in India.
   d) Sent by → Hand delivery or by post or by courier, or through such electronic means as may be prescribed.
   e) Approved if → Approved by a majority of the directors or members, who are entitled to vote on the resolution.
   f) Provided that, where minimum one-third of the total 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.

2. A resolution under sub-section (1) shall be noted at a subsequent meeting of the Board and made part of the minutes of such meeting.

Question 13.
How is a resolution by circulation passed by the Board or its Committee.

Answer
1. The Companies Act, 2013 permits a decision of the Board of Directors to be taken by means of a resolution by circulation. Board approvals can be taken in one of the 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 have been complied with:
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(a) the resolution has been circulated in draft, together with the necessary papers, if any,
(b) the draft resolution has been circulated to all the directors, or members of the committee, as the case may be;
(c) the Draft resolution has been sent at their addresses registered with the company in India;
(d) such delivery has been made by hand or by post or by courier, or through prescribed electronic means;
(e) such resolution has been approved by a majority of the directors or members, who are entitled to vote on the resolution;

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.

2. However, if at least 1/3rd of third 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).

3. A resolution that has been passed by circulation shall have to be necessarily be noted in the next meeting of board or the committee, as the case may be, and made part of the minutes of such meeting.

Question 14

Some urgent items are left over in the agenda of Board meeting which concluded and decision cannot be deferred till its next meeting. Advice the company about how the resolution shall be passed now.

Answer

Resolutions may be passed in resect of Board approvals in one of the two ways, either at the board meetings or by circulation. The items which could not be concluded and decided at the board meeting, if cannot be deferred till the next meeting may be passed by circulation, provided they do not include such items as are required to be passed only at the meeting of the directors under section 179(3) of the Companies Act, 2013.

In order to pass any resolution of the Board by circulation the following steps must be taken and completed as laid down in section 175(1):
(a) The draft of the proposed resolution must be circulated along with all relevant and necessary papers;
(b) The above documents must be delivered to all the directors, members or the committee, as the case may be, at their addresses registered with the company in India;
(c) The documents must be delivered by hand delivery or by post or by courier, or through such electronic means as may be prescribed;
(d) The resolution must be approved by a majority of the directors or members, who are entitled to vote on the resolution.
(e) There must not be any objection from not less than one-third of the total number of directors of the company for the time being, requiring that such resolution under circulation must be decided at a meeting.

Further, the resolution so passed shall be noted at a subsequent meeting of the Board or the committee thereof, and be made part of minutes of such meeting.

Question 15
In the course of administration of the affairs of a limited company, Chairman of the Board of directors came across a matter which required the approval by way of a board resolution. In the prevailing circumstances, it is not possible to convene and hold a Board meeting. The chairman approaches you to advise him of the way and the relevant procedure to obtain such approval without holding the Board meeting. Advise the chairman, taking into account the relevant provisions of the Companies Act, 2013

Answer

Passing of Resolution by Circulation:
Resolutions may be passed in resect of Board approvals in one of the two ways, either at the board meetings or by circulation. Only those board resolutions may be passed by circulation, that do not relate to such items as are required to be passed only at the meeting of the directors under section 179(3) of the Companies Act, 2013.

In order to pass any resolution of the Board by circulation the following steps must be taken and completed as laid down in section 175(1):

(a) The draft of the proposed resolution must be circulated along with all relevant and necessary papers;
(b) The above documents must be delivered to all the directors, members or the committee, as the case may be, at their addresses registered with the company in India;
(c) The documents must be delivered by hand delivery or by post or by courier, or through such electronic means as may be prescribed;
(d) The resolution must be approved by a majority of the directors or members, who are entitled to vote on the resolution.
(e) There must not be any objection from not less than one-third of the total number of directors of the company for the time being, requiring that such resolution under circulation must be decided at a meeting.

Further in terms of section 175(2) of the Companies Act, 2013 a resolution passed by circulation under section 175(1) shall be noted at a subsequent meeting of the Board or the committee thereof, as the case may be, and made part of the minutes of such meeting.

SECTION 176: DEFECTS IN APPOINTMENT OF DIRECTOR NOT TO INVALIDATE ACTIONS TAKEN BY DIRECTORS.

1. When after appointment of a director, it is subsequently noticed that his appointment was invalid by reason of any defect or disqualification contained in this Act or in the articles of the company, All acts done by such director PRIOR TO showing of such defect shall continue to remain VALID.

2. But All acts done by such director AFTER showing of such defect shall be INVALID.

Question 16
State whether the acts done by the Board meeting be invalid if it was found afterwards that there was some defect in the appointment of directors or any person acting as a director?

Answer
Under section 176 of the Companies Act, 2013 no act done by a person as a director shall be deemed to be invalid, notwithstanding that it was subsequently noticed that his appointment was invalid by reason of any defect or disqualification or had terminated by virtue of any provision contained in this Act or in the articles of the company.

Provided that nothing in this section shall 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.

Therefore, from the above provisions of law, all acts done by the Board meeting or by its committee meeting or by any person acting as a director shall be as valid as if every such director or such person had been duly appointed and was qualified to be a director. The validity of all such acts done is not affected even if it discovered later on that there was some defect in the appointment of any one or more of such directors or of any person acting as a director.

However, once the defect in appointment is noticed by the company, no such acts of the director will be valid.

**Question 17**

Mr. MTP was appointed as a director at the Annual General Meeting of a limited company held on 30th September, 2013 and he carried on his duties and functions as a director. In the month of August, 2014, it was found out that there were certain irregularities in his appointment and on 31st August, 2014, his appointment was declared invalid. But Mr. MTP continued to act as director even after 31st August, 2014. You are required to state, with reference to the provisions of the Companies Act, 2013, whether the acts done by Mr. MTP are valid and binding upon the company?

**Answer**

In accordance with section 176 of the Companies Act, 2013 acts done by a person as a director shall be deemed to be valid, notwithstanding that it may afterwards be discovered that his appointment was invalid by reason of any defect or disqualification or had terminated by virtue of any provision contained in this Act or in the articles of the company.

The Proviso to section 176 further provide that nothing in this section shall be deemed to give validity to acts done by a director after his appointment has been noticed by the company to be invalid or to have terminated.

In view of the above provisions of section 176 of the Companies Act, 2013, the acts done by Mr. MTP up to the date of the irregularity in his appointment coming to the notice of the company will be deemed as valid and binding on the Company.

Any act done by him after the date on which the irregularity or defect in his appointment was noticed by the company will be deemed invalid. The acts done by Mr. MTP after 31st August, 2014 shall be deemed to be invalid and not binding upon the Company.

**SECTION 177 : AUDIT COMMITTEE**

1. **FORMATION OF AUDIT COMMITTEE**

   Audit committee must be constituted by the Board of Directors of:
   
   a) **Every listed company**
      
      And
   
   b) **Such other** class or classes of companies, as may be prescribed, shall constitute an audit Committee.
Rule 6 of the Companies (Meeting of Board and its Powers) Rules, 2014 have prescribed the following classes of companies which shall have to constitute an Audit committee:

i) All public companies with PUSC of ₹ 10 crore or more.# 
ii) All public companies having turnover of ₹ 100 crore or more.#
iii) All public companies having in aggregate, Outstanding Loans or Borrowings or Debentures or Deposits Exceeding ₹ 50 crore.#

# → As on the date of last audited financial statements.

2. **COMPOSITION:**
The Audit Committee shall consist of
a) A **minimum** of three directors
b) With independent directors forming a **majority.** (*Not applicable to Section 8 Companies*)
c) Provided that **majority** of members of Audit Committee including its Chairperson must be persons financially literate.

d) Every Audit Committee of a company existing immediately before the commencement of this Act must be reconstituted in accordance with rules of this act **within one year** of such commencement.

**Exemptions:**

Vide Notification G.S.R. 466(E) ‘Independent Directors forming a majority’ is omitted in constitution of audit committee for the Companies covered under Section 8 of the Companies Act, 2013.

3. **FUNCTIONS OF AUDIT COMMITTEE:**
As specified in writing by the Board, including,—
a) The recommendation for appointment, remuneration and terms of appointment of
In case of Government companies, in this clause, for the word “recommendation for appointment, remuneration and terms of appointment” the words “recommendation for remuneration” shall be substituted- Vide Notification no. G.S.R. 463(E), dated 5.6.15.

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;

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 inserted by Companies (Meeting of Board and its powers) Second Amendment Rules, 2015;

The Audit Committee may make omnibus approval for related party transactions proposed to be entered into by the company subject to such conditions as may be prescribed.

In case of transaction, other than transactions referred to in section 188, and where Audit Committee does not approve the transaction, it shall make its recommendations to the Board.

In case any transaction involving any amount not exceeding one crore rupees is entered into by a director or officer of the company without obtaining the approval of the Audit Committee and it is not ratified by the Audit Committee within three months from the date of the transaction, such transaction shall be voidable at the option of the Audit Committee and if the transaction is with the related party to any director or is authorised by any other director, the director concerned shall indemnify the company against any loss incurred by it.

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.

4. RESPONSIBILITIES OF AUDIT COMMITTEE:

The Audit Committee may call for the comments of the auditors about:

a) Internal control systems,

b) Scope of audit,

c) Observations of the auditors.

d) Review of financial statement before their submission to the Board.

e) Any other related issues with the internal and statutory auditors of the company.
5. **AUTHORITY TO INVESTIGATE:**
   The Audit Committee shall have authority to investigate into any matter related to its functions 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.

6. **ROLE OF AUDITOR IN 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 auditors report but shall not have the right to vote.

7. **DISCLOSURE IN BOARD REPORT:**
   The Board’s report under sub-section (3) of section 134 must disclose the composition of an Audit Committee and Where the Board had not accepted any recommendation of the Audit Committee, the same must be disclosed in such report along with the reasons.

8. **VIGIL MECHANISM:**
   (i) **Formation of Vigil Mechanism:**
   Every listed company or such class or classes of companies, as may be prescribed, must establish a vigil mechanism for directors and employees to report genuine concerns in such manner as may be prescribed.

   **Rule 7 of the Companies (Meeting of Board and its Powers) Rules, 2014** have prescribed the following classes of companies which shall have to set up a vigil mechanism:

   a) A company which accepts Public deposits.
   b) A company which has borrowed money from banks and public financial institutions in excess of ₹ 50 Crore.

   (ii) **Objective of formation of vigil mechanism:**
   A vigil mechanism shall be formed for directors and employees to report genuine concerns in such manner as prescribed in Rule 7 of the Companies (Meetings of Board and its Powers)
(iii) Safeguards against victimization:

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) Disclosure about establishment of the Mechanism:

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.

According to Rule 7 of the Companies (Meetings of Board and its Powers) Rules, 2014:

1) “Persons who use such mechanism” means employees and directors who avail the vigil mechanism.

2) 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) 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 to whom other directors and employees may report their concerns.

4) 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.

5) 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.

Note: In the case of Listed company formation, composition, responsibilities and rights of Audit committee shall be governed by SEBI (LODR) Regulations issued under SEBI Act, 1992.

Question 18

An Audit Committee of a Public Limited Company constituted under section 177 of the Companies Act, 2013 submitted its report of its recommendation 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 be Board resort to?

Answer

(a) As per Section 177(2) and (3) of the Companies Act, 2013 an audit committee must be formed within a year of the commencement of the Act or within a year of the incorporation of a company as the case may be, and will consist of at least 3 directors out of which the independent directors shall constitute the majority.

Under section 177(8) the Board’s Report which is laid before a general meeting of the company under section 134 (3) where the financial statements of the company are placed before the members, must disclose the
composition of the audit committee and also where the Board has not accepted any recommendations of the audit Committee the same shall be disclosed alongwith the reasons therefor. Therfore, the Board is empowered not to accept the recommendations of the Audit Committee but only under genuine circumstances and with legitimate reasons.

(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) placed before a general meeting of the company.

**Question 19**

MNC Ltd., a company, whose paid up capital was ₹ 4.00 Crores, has issued rights 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.

**Answer**

Under section 177(1) of the Companies Act, 2013 the Board of Directors of every listed company and such other class or classes of companies, as may be prescribed, shall constitute an Audit Committee. 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, the majority of 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 -- Director nominated by IDBI
4. Mr. D -- An Independent Director
5. Mr. FD – An Independent Director
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.”

Question 20
Supra Limited, a private company, has been converted into a public company and under the provision of the of the Companies Act, 2013. The company proposes to constitute an audit committee. Taking into account the provisions of the Companies Act, 2013 draft a board resolution covering the following matters:
(i) Member of the audit committee.
(ii) Chairman of the audit committee.
(iii) Any two functions of the said committee.

Answer
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. ---- Nominee of IDBI
2. Mr. ---- Independent Director
3. Mr. ---- Independent Director
4. Mr. ---- Independent Director
5. Mr. ---- Independent 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”.

Question 21

Explain how the provisions of the Companies Act, 2013 relating to Audit Committee will help in achieving some of the objectives of Corporate Governance.

Answer

Companies, particularly public listed companies raise huge amounts of monies from the members of the public and public financial institutions. They owe it to all the vast number of persons and institutions who have reposed their faith in them and have invested in them, that their faith is rewarded both in terms of annual return and in terms of wealth appreciation in real terms. In order to achieve this it is vital to have the highest quality of corporate governance in the conduct of affairs of such companies. Thus, the role of audit committees have been enhanced, their responsibilities made more objective and the accountability has increased substantially.

In this context the provisions of the Companies Act, 2013 have been framed to improve corporate governance standards and protect the interests of the public and the financial institutions who have invested in companies. These provisions may be highlighted as under:

1. The constitution of Audit Committees under section 177(2) requires the majority representation from independent directors. In other words, persons from within the management cannot form a majority in the Committee, thereby making the functioning of these committees more transparent;

2. The proviso to section 177(2) further requires the majority of members and the chairperson of the Audit Committees to be persons who can understand financial statements. This enables a meaningful exercise of the committee’s functions by knowledgable persons thereby increasing the effectiveness of such committees.

3. Now the terms of reference or the minimum scope of work of an Audit Committee has been laid down in the act itself under section 177(4). By doing this the vagueness and doubt in the role and functions of such committees has been removed.

4. The Audit Committee shall have authority to investigate into any matter in relation to the areas of its scope of functioning or referred to it by the Board and for this shall have power to obtain professional advice from external sources and have full access to information contained in the records of the company. This provides the Audit Committee to function with a high degree of effectiveness by accessing external professional advice and the records of the company.

5. The recommendations of the Audit Committee are binding on the Board to take appropriate corrective actions. In case the Board of Director refuses to accept the recommendations of the Audit Committee, it bound
to disclose the same with the reasons for non acceptance, in its report to the members of the company under section 134 (3) which relates to the Directors Report on Financial Statements to the members of the company. It will be seen from the above provisions of the Companies Act, 2013 that efforts have been made to make such committees more impartial, effective and accountable which will enable to company to improve the quality of its corporate governance thereby improving accountability and avoiding financial impropriety.

Question 22
(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) Member 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 not restricted under Section 144?

Answer
(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. ---- Independent 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 have prescribed that the following classes of companies shall constitute Audit Committee:
(a) all public companies with a paid up capital of 10 crore rupees or more;
(b) all public companies having turnover of 100 crore rupees or more;
(c) all public companies, having in aggregate, outstanding loans or borrowings or debentures or deposits exceeding 50 crore rupees or more. Hence, in the present question, the likely turnover 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.

SECTION 178 : NOMINATION and REMUNERATION COMMITTEE and STAKE HOLDERS RELATIONSHIP COMMITTEE.

(1) REQUIREMENTS AS TO WHEN TO FORM and WHO ALL TO BE MEMBERS.

- The Board of Directors of every listed company
- and such other class or classes of companies, as may be prescribed
- shall constitute the Nomination and Remuneration Committee
- consisting of three or more non-executive directors
- out of which not less than one-half shall be independent directors.

Provided that the chairperson of the company (whether executive or non-executive) may be appointed as a member of the Nomination and Remuneration Committee but shall not chair such Committee.

Companies (Meeting of Board and its Powers) Rules, 2014 have prescribed the following classes of companies which shall have to constitute an Audit committee:

i) All public companies with PUSC of ₹ 10 crore or more.#

ii) All public companies having turnover of ₹ 100 crore or more.#

iii) All public companies having in aggregate, Outstanding Loans or Borrowings or Debentures or Deposits Exceeding ₹ 50 crore.#

# → As on the date of last audited financial statements.

Exemptions:

This section 178 shall not apply to the Companies covered under section 8 of the Companies Act, 2013.

In case of Specified IFSC Public Company - Section 178 shall not apply. - Notification Dated 4th January 2017.

(2) The Nomination and Remuneration Committee shall

- identify persons who are qualified to become directors and
- who may be appointed in senior management,
- recommend to the Board their appointment and removal and
shall carry out evaluation of every director’s performance.

(3) The Nomination and Remuneration Committee shall
➢ formulate the criteria and policy for determining qualifications, etc of a director and
➢ recommend to the Board a policy relating to the remuneration.
➢ Such policy shall also be disclosed in the Board's report.

Note: In the case of Listed company formation, composition, responsibilities and rights of Nomination and Remuneration committee shall be governed by SEBI (LODR) Regulations issued under SEBI Act, 1992.

(4) STAKEHOLDERS RELATIONSHIP COMMITTEE
➢ A company which consists of more than one thousand shareholders/ debenture-holders/ deposit-holders / any other security holders at any time during a financial year
➢ must constitute a Stakeholders Relationship Committee
➢ consisting of a chairperson who must be a non-executive director
➢ and other members as decided by the Board.

(5) The Stakeholders Relationship Committee shall consider and resolve the grievances of security holders of the company.

(6) In case of any contravention,
➢ The company shall be punishable with fine
   One lakh rupees upto Five lakh rupees ( ₹ 1,00,000/- to ₹ 5,00,000/-) and
➢ Every officer of the company who is in default shall be punishable with
   Imprisonment : upto 1 year
   or
   fine : Twenty-five thousand rupees upto One lakh rupees, ( ₹ 25,000/- to ₹ 1,00,000/-)
   or
   with Both

(7) Provided that non-consideration of any grievance by the Stakeholders Relationship Committee in good faith shall not constitute a contravention of this section.

Note: In the case of Listed company formation, composition, responsibilities and rights of Stakeholder Relationship committee shall be governed by SEBI (LODR) Regulations issued under SEBI Act, 1992.

Question 23
Referring to the provisions of the Companies Act, 2013, answer the following:
(A) Which companies are required to constitute a ‘Nomination and Remuneration Committee’?
(B) What is the composition of the above committee?
Answer

(A) Formation of Nomination and Remuneration Committee: As per the provisions of Section 178 of the Companies Act, 2013, a Nomination and Remuneration Committee shall be constituted by the Board of Directors of:
(a) Every listed company and
(b) Such other class or classes of companies as may be provided.
The Companies (Meetings of Board and its powers) Rules, 2014, has prescribed the following classes of companies that shall constitute Nomination and Remuneration Committee of the Board:
(1) All public companies with a paid up capital of 10 crore rupees or more;
(2) All public companies having a turnover of one hundred crore rupees or more;
(3) All public companies, having in aggregate, outstanding loans or borrowings or debentures or deposits exceeding fifty crore rupees or more.
Explanation – The paid up share capital or turnover or outstanding loans, or borrowings or debentures or deposits, as the case may be, as existing on the date of last audited Financial Statements shall be taken into account for the purposes of this rule.
Provided further that public companies covered under this rule shall constitute their Nomination and Remuneration Committee within one year from the commencement of these rules or appointment of independent directors by them, whichever is earlier.

(B) Composition of Nomination and Remuneration Committee:
(a) This committee shall consist of 3 or more non-executive directors out of which not less than one-half shall be independent directors.
(b) The Chairman (whether executive or non-executive) of the company shall not chair such a committee. However, he may be appointed as a member to the committee.
(c) The chairperson or in his absence, any other member of the committee authorized by him in this behalf shall attend the general meetings of the company.

SECTION 179 : POWERS OF BOARD.

(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 authorised to exercise and do. (Subject to Act, MOA, AOA and regulations)

(2) The Board shall not exercise any power or do any act or thing which is directed or required, to be exercised or done by the company in general meeting. i.e. powers of shareholders cannot be exercised by BOD.

(3) Any regulation made by the company in general meeting shall not invalidate any prior act of the Board.

(4) The Board of Directors of a company shall exercise the following powers ONLY AT A BOARD MEETING (i.e. resolution by circulation not allowed for these), namely:— [Section 179(3)]

AB²C DIL FROG
(a) to take over a company or **acquire** a controlling or substantial stake in another company;
(b) to authorise **buy-back** of securities under section 68;
(c) to borrow monies;
(d) to make **calls** on shareholders in respect of money unpaid on their shares;
(e) to issue securities, including **debentures**, whether in or outside India;
(f) to invest the funds of the company;
(g) to grant **loans**;
(h) to approve **financial statement** and the Board’s report;
(i) to approve amalgamation, merger or **reconstruction**, to diversify the business of the company;
(j) any **other** matter which may be prescribed in Rule 8 of the Companies (Meetings of Board and its Powers) Rules, 2014: **PAA**

→ Political Contribution u/s/ 182
→ Appointment and removal of key managerial personnel.
→ Appointment of Internal Auditor and Secretarial Auditor.

(k) to give **guarantee** or provide security in respect of loans

The Board may delegate to any committee of directors, the managing director, the manager or any other officer the powers specified in points (c) (f) (g) (k) on such conditions as it may specify by a resolution passed at a meeting

---

**Exemptions:**

Matters referred to in clauses (c), (f), (g) and (k) of sub-section (3) of section 179 may be decided by the board by circulation instead of at a meeting in respect to the companies covered under section 8 of the Companies Act, 2013.

In case of **Specified IFSC Public Company and IFSC Private Company** - In sub-section (3) of Section 179, after the second proviso, the following proviso shall be inserted, namely:-

“Provided also that in case of a Specified IFSC public company and IFSC Private Company, the Board can exercise powers by means of resolutions passed at the meetings of the Board or through resolutions passed by circulation.”. Notification Dated 4th January 2017.

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**Exemption to banking companies:** However, the acceptance by a banking company in the ordinary course of its business of deposits of money from the public repayable on demand or otherwise and withdrawable by cheque, draft, order or otherwise, or 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 borrowing of monies or, as the case may be, a making of loans by a banking company within the meaning of this section.

**Explanation I**—Nothing in point (d) above shall 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.

**Explanation II**—In respect of dealings between a company and its bankers, the exercise by the company of the power specified in point (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 and not 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.

(5) The members of company can impose restrictions and conditions on the exercise by the Board of any of the powers by passing a resolution at general meeting.

Question 24
Out of the powers exercisable by the Board under section 179, the board wants to delegate to the Managing Director of the company the power to borrow monies otherwise than on debentures. Advise whether such a delegation is possible? Would your answer be different, if the delegation is given to the manager or any other principal officer including a branch officer of the company?

Answer
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 above provisions it is clear that the power to borrow monies under (d) above, may be delegated to the Managing Director or to the manager or any other principal officer of the company. However, the power to borrow monies on behalf of the company cannot be delegated to a branch officer (principal officer of the branch) unless the borrowing is related to the requirements of the functioning of the branch office.

Question 25
A Managing Director was authorized by the Board to borrow money on a Promissory Note. State in this connection whether borrowing on a promissory note is within the powers of the directors.

Answer
In terms of section 179(3)(d) the board of directors is required to exercise the power of borrowing monies only by means of a resolution passed at a duly convened Board Meeting. The proviso to section 179 further iterates
that the Board may by means of a resolution passed at a Board Meeting delegate this power to the Managing Director. The section does not describe the modus operandi of the borrowing transaction.

From the above provisions, it is clear that the Board may delegate the power to borrow against promissory note.

It should be noted however, that the requirement of approval of the company, if applicable will have to be met and such approval taken. Delegation to the Managing Director merely covers the part of Board approval and all further approval as required by Companies Act will have to be taken.

It has been held in [P. Rangaswami Reddiar and Another vs. R. Krishnaswami Reddiar and another (1971) 43 Comp. Case 232] that where such a borrowing permissible under the company’s articles and moneys were borrowed on promissory notes, such transaction would come within the powers of the directors. It has also been held in the same case that where a person was appointed as the managing director of the company by the Board’s resolution vested with full powers of the management of the affairs of the company and authorised to sign all the papers of the company, he would have full powers to borrow money on a promissory note even without a resolution of the Board as contemplated by Section 292(c) of the Companies Act, 1956. This same ruling can be applied for section 179(3)(d) of the Companies Act, 2013 also.

Question 26

Advise the Board of Director of Spectra Papers Ltd. regarding validity and extent of their powers, under the provisions of the Companies Act, 2013 in relation to the following matters:

(i) Buy-back of the shares of the Company, for the first time, upto 10% of the paid up equity share capital without passing a special resolution.

(ii) Delegation of Power to the Managing Director of the company to invest surplus funds of the company in the shares of some companies.

Answer

(i) According to clause (b) of section 179(3), The Board of Directors of a company shall exercise the power to authorise 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.

Thus, we can say that in the case of buy-back of shares of the Company, for the first time, upto 10% of the 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.

(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 meetings of the Board
The board may under the proviso to section 179(3) of the Companies Act, 2013 delegate the power to invest the funds of the company by a Board Resolution passed at a duly convened Board Meeting. However, the investment in shares of other companies will be governed by the applicable provisions of the Companies Act, 2013 (i.e. section 186 of the Companies Act, 2013). Since the investment of funds is governed by section of the Companies Act, 2013, thus, specific provisions of section 186 will be applicable for such investment. According to section 186(5), 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. 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.

SECTION 180 : RESTRICTIONS ON POWERS OF BOARD.

Exemptions:
This section is not applicable to Private company as per the Notification no. 464(E), dated 5th June 2015.
In case of Specified IFSC Public Company - Section 180 Shall apply in case of a Specified IFSC public company, unless the articles of the company provides otherwise - Notification Dated 4th January 2017.

1) The Board of Directors of a company shall exercise the following powers only with the consent of the company by a SPECIAL RESOLUTION :

**Board Is Restricted to Sell**

<table>
<thead>
<tr>
<th>RESTRICTION</th>
<th>CONDITION</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) to <strong>borrow</strong> money,</td>
<td>where the money to be borrowed, together with the money already borrowed by the company will exceed aggregate of its paid-up share capital and free reserves, apart from temporary loans obtained from the company’s bankers in the ordinary course of business:</td>
</tr>
</tbody>
</table>

i.e. \( \{ \text{Already borrowed} + \text{proposed to be borrowed} \} > \{ \text{PUSC} + \text{FR} + \text{SECURITIES PREMIUM ( Amendment)} \} \)

Explanation.—For the purposes of this clause, the expression “temporary loans” means loans
repayable on demand or within six months from the date of the loan such as short-term, cash credit arrangements, the discounting of bills and the issue of other short-term loans of a seasonal character, but does not include loans raised for the purpose of financial expenditure of a capital nature;

(b) to **invest** otherwise in trust securitiesthe amount of compensation received by it as a result of any merger or amalgamation;

(c) to **remit**, or give time for the repayment of, any debt due from a director.

(d) to **sell**, lease or otherwise dispose of the whole or substantially the whole of the undertaking of the company

Explanation.—For the purposes of this clause,—

(i) “undertaking” means

➔ an undertaking in which the investment of the company exceeds 20% of its net worth * or

➔ an undertaking which generates 20% of the total income of the company during the previous financial year;

(ii) the expression “substantially the whole of the undertaking” in any financial year means 20% or more of the value of the undertaking *;

* as per the audited balance sheet of the preceding financial year.

2) **Exception:**

Nothing contained in above point (d) with respect to sell, lease or otherwise dispose of the whole or substantially the whole of the undertaking of the company shall affect—

a. the title of a buyer or other person who buys or takes on lease any property, investment or undertaking as is referred to in that clause, in good faith; or

b. The sale or lease of any property of the company where the ordinary business of the company consists of, or comprises, such selling or leasing.

3) **Imposition of condition:**

Any special resolution passed by the company consenting to the transaction as is referred to in above point (d) may stipulate such conditions as may be specified in such resolution, including conditions regarding the use, disposal or investment of the sale proceeds which may result from the transactions.

Exemption: Provided that, this sub section shall not be deemed to authorise the company to effect any reduction in its capital except in accordance with the provisions contained in this Act.

4) Every special resolution passed by the company in general meeting in relation to borrowings shall specify the total amount up to which monies may be borrowed by the Board of Directors.
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CA Adithi S. Chaturvedi.

5) A debt incurred by the company in excess of the limit imposed by clause on borrowing shall not be valid or effectual, unless the lender proves that
   → He advanced the loan in good faith and
   → without knowledge that the limit imposed by that clause had been exceeded.

Question 27
M/s ABC Ltd. had power under its memorandum to sell its undertaking to another company having similar objects. The Articles of the company contained a provision by which directors were empowered to sell or otherwise deal with the property of the company. The Shareholders passed an ordinary resolution for the sale of its assets on certain terms and required the directors to carry out the sale. The Directors refused to comply with the wishes of the shareholders where upon it was contended on behalf on the shareholders that they were the principal and directors being their agents were bound to give effect to their decision. Based on the above facts, decide the following issues, having regard to the provisions of the Companies Act, 2013 and case laws.

(i) Whether the contention of shareholders against the non-compliance of their wishes by the directors is tenable.
(ii) Can shareholders usurp the powers which by the articles are vested in the directors by passing a resolution in the general meeting?

Answer
According to 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 authorised 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 memorandum or articles of the company or otherwise, to be exercised or done by the company in general meeting.

The Companies Act, 2013 vide section 180 (1) lays down the powers of the Board of Directors of a company which can be exercised 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 of 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 the members of the company accorded vide 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 by 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 the members to have the proposal approved by a special resolution.

In the given case therefore, the procedure followed is completely incorrect. The shareholders cannot on their own make out a proposal of sale and pass an ordinary resolution to implement it through the directors.
Therefore, the contention of the shareholders is incorrect in the first place as it is not within their authority to approve a proposal independently of the Board of Directors. It is for the Board to approve a proposal of sale of the undertaking and then get the members to approve it by a special resolution. Further, in exercising their powers the directors do not act as agent for the majority members or even 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.

**Question 28**

The Board of Directors of Stepping Stones Publications Ltd. at a meeting held on 15.1.2014 resolved to borrow a sum of ₹ 15 crores from a nationalized bank. Subsequently the said amount was received by the company. 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 powers of the Board of Directors. The Company seeks your advice and the following data is given for your information:

(i) Share Capital ₹ 5 crores
(ii) Reserves and Surplus ₹ 5 crores
(iii) Secured Loans ₹ 15 crores
(iv) Unsecured Loans ₹ 5 crores

**Advice the management of the company.**

**Answer**

According to the provisions of Section 180(1)(c) of the Companies Act, 2013, there are restrictions on the borrowing powers to be exercised by the Board of directors. According to the said section, the borrowings should not exceed the aggregate of the paid up capital and free reserves. 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 crores will exceed the limit mentioned. Thus, the borrowing will be beyond the powers of the Board of directors.

Thus, the management of Stepping Stone Publications Ltd., 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 the borrowing will be valid and binding on the company and its members.

**Question 29**

Following is data relating to Prince Company Limited:

Authorised Capital (Equity Shares) ₹ 100 crores
Paid – up Share Capital 40 crores
General Reserves20 crores
Debenture Redemption Reserve 10 crores
Provision for Taxation 5 crores
Loan (Long Term) 10 crores
Short Term Creditors 3 crores

Board of Directors of the company by a resolution passed at its meeting decided to borrow an additional sum of ₹ 90 crores from the company’s Bankers. You being the company’s financial advisor, advise the Board of Directors the procedure to be followed as required under the Companies Act, 2013.
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 up to an amount which does not exceed the aggregate of paid up capital of the company and its free reserves. 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, up to an amount calculated as follows:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>₹ in crores</th>
</tr>
</thead>
<tbody>
<tr>
<td>Paid up Share Capital</td>
<td>40</td>
</tr>
<tr>
<td>General Reserve (being free reserve)</td>
<td>20</td>
</tr>
<tr>
<td>Debenture Redemption Reserve (This reserve is not to be considered since it is kept apart for specific purpose of debenture redemption)</td>
<td>---</td>
</tr>
</tbody>
</table>

**Aggregate of paid up capital and free reserve.**

| Total borrowing power of the Board of Directors of the company, i.e, 100% of the aggregate of paid up capital and free reserves | 60          |
| Less: Amount already borrowed as Long term loan | 10          |

**Amount upto which the Board of Directors can further borrow without the approval of shareholders in a general meeting.**

|                                                  | 50          |

In the present case, the directors of Prince Company Limited by a resolution passed at its meeting decide to borrow an additional sum of ₹ 90 Crore from the company bankers. Thus, the borrowing will be beyond the powers of the Board of directors.

Thus, the management of Prince Company Limited, 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, the borrowing will be valid and binding on the company and its members.

[Note: In case of private companies section 180 shall not apply vide Notification no. G.S.R. 464(E), dated 5th June 2015]

Question 30

One of the Objects Clauses of the Memorandum of Association of Info Company 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 where upon 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 usurp the powers which by the Articles are vested in the directors by passing a resolution in the general meeting?

Answer

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 there under 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, provides that the powers of the Board of Directors of a company which can be exercised 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 vide 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 Act. 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 independently of the Board of Directors. It is for the Board to approve a proposal of sale of the undertaking and then get the members to approve it by a special resolution. Accordingly the contention of the members that they were the principals and directors being 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 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.

SECTION 181 : CONTRIBUTION TO CHARITABLE FUNDS.

(1) The Board of Directors of a company may contribute to bona fide charitable and other funds without any permission from shareholders till contribution does not exceed 5% of its average net
profits for the three immediately preceding financial years.

(2) Prior permission of Shareholders shall be required for such contribution in case the aggregate amount, in any financial year, exceeds 5% of its average net profits for the three immediately preceding financial years.

Question 31

The Board of directors of Very Well Ltd., are 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. In this connection, state whether the directors can do so?

Answer

Under section 181 of the Companies Act, 2013 the Board of Directors of a company is authorised 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 a financial year. As the amount of donation is restricted to the average of previous 3 years’ profits, it is possible for a company suffering a loss to make a contribution provided it is to a bonafide charitable fund.

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 upto the average of the preceding three years’ profits. In case the contribution exceeds the limit, the approval of the members must be taken at a general meeting of the company.

Question 32

The last three years’ Balance Sheet of PTL Ltd., contains the following information and figures:

<table>
<thead>
<tr>
<th></th>
<th>As at 31.03.2012</th>
<th>As at 31.03.2013</th>
<th>As at 31.03.2014</th>
</tr>
</thead>
<tbody>
<tr>
<td>Paid up capital</td>
<td>50,00,000</td>
<td>50,00,000</td>
<td>75,00,000</td>
</tr>
<tr>
<td>General Reserve</td>
<td>40,00,000</td>
<td>42,50,000</td>
<td>50,00,000</td>
</tr>
<tr>
<td>Credit Balance in</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Profit and Loss Account</td>
<td>5,00,000</td>
<td>7,50,000</td>
<td>10,00,000</td>
</tr>
<tr>
<td>Debenture Redemption Reserve</td>
<td>15,00,000</td>
<td>20,00,000</td>
<td>25,00,000</td>
</tr>
<tr>
<td>Secured Loans</td>
<td>10,00,000</td>
<td>15,00,000</td>
<td>30,00,000</td>
</tr>
</tbody>
</table>

On going through other records of the Company, the following is also determined:

Net Profit for the year 12,50,000 19,00,000 34,50,000

(as calculated in accordance with the provisions of the Companies Act, 2013)

In the ensuing Board Meeting scheduled to be held on 5th November, 2014, 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 2014-15 without seeking the approval in general meeting.

Answer

(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 and its free reserves. Such borrowing shall not include temporary loans obtained from the company’s bankers in 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 November, 2014, the figures relevant for this purpose are the figures as per the Balance Sheet as at 31.03.2014. 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:

- **Paid up Capital** 75,00,000
- **General Reserve (being free reserve)** 50,00,000
- **Credit Balance in Profit and 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) -----

Aggregate of paid up capital and free reserve 1,35,00,000

Total borrowing power of the Board of Directors of the company, i.e, 100% of the aggregate of paid up capital and free reserves 1,35,00,000

Less: Amount already borrowed as secured loans 30,00,000

Amount upto which the Board of Directors can further borrow without 1,05,00,000 the approval of shareholders in a general meeting.

(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):
- For the financial year ended 31.12.2011 12,50,000
- For the financial year ended 31.12.2012 19,00,000
- For the financial year ended 31.12.2013 34,50,000
TOTAL
Average of net profits during three preceding financial years 22,00,000
Five per cent thereof 1,10,000

Hence, the maximum amount that can be donated by the Board of Directors to a genuine charitable fund by PTL Ltd during the financial year 2013-14 will be Rs 1,10,000 without seeking the approval of the shareholders in a general meeting.

SECTION 182: POLITICAL CONTRIBUTIONS.

(1) **WHO CANNOT CONTRIBUTE?**
   a) A Government company and
   b) A company which has been in existence for less than three financial years.

(2) **POLITICAL CONTRIBUTION:**
   Contribution of any amount directly or indirectly to any political party.

(3) **REQUIREMENT FOR MAKING CONTRIBUTION:**
   Such contribution shall be made by a company only after passing a resolution authorising the contribution at a Board meeting and such resolution shall be deemed to be justification in law for the making and the acceptance of the contribution authorised by it.

(4) **CONTRIBUTIONS WHICH SHALL BE DEEMED TO BE INDIRECT CONTRIBUTION TO POLITICAL PARTY:**
   (a) A donation or subscription or payment given by a company on its behalf which can reasonably be regarded as likely to affect public support for a political party shall also be deemed to be contribution for a political purpose;

   (b) the amount of expenditure incurred, directly or indirectly, by a company on an advertisement in any publication, being a publication in the nature of a souvenir, brochure, tract, pamphlet or the like, shall also be deemed,—

   (i) where such publication is by or on behalf of a political party, to be a contribution of such amount to such political party, and
   (ii) where such publication is not by or on behalf of, but for the advantage of a political party, to be a contribution for a political purpose.

(5) **DISCLOSURE IN BOOKS OF ACCOUNTS:**
   Every company shall disclose in its profit and loss account any amount or amounts contributed by it to any political party during the financial year to which that account relates.

(6) **MODE OF CONTRIBUTION:** *
   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.

Provided that 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.”[Section 182(3A)]

★ This section 3A has been inserted vide Finance Act, 2017, w.e.f. 31.3.2017.

(7) **CONTRAVENTION:**
If a company makes any contribution in contravention of the provisions of this section,

the company shall be punishable with fine

which may extend to **five times** the amount so contributed

AND

every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to **six months** and

with fine which may extend to **five times** the amount so contributed.

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**The MCA vide General Circular 19/ 2013 dated 10th December 2013, issued a clarification on disclosures to be made under section 182 relating to ‘Prohibition and restrictions regarding political contributions’ of the Companies Act, 2013.**

The circular says that, with the coming into force of the scheme relating to 'Electoral Trust Companies' under 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 be sufficient, 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.
**Question 33**
The Board of Directors of LM Limited propose to donate ₹ 50,000 to a political party during the Financial year ending 31st March, 2014. The average net profits determined in accordance with the provisions of the Companies Act, 2013 during the immediately preceding three financial years is ₹ 40,00,000. Examine with reference to the provisions of the Companies Act, 2013 whether the proposed donation is within the power of the Board of Directors of company.

**Answer**
Donation to political parties: Under section 182(1) of the Companies Act, 2013 a company may contribute any amount directly or indirectly to any political party, unless it is a Government Company and a company which has been in existence for less than three financial years. In the given case LM Ltd it is presumed to be a non government company. The contribution is well within the power of the Board of Directors of the company. Hence, the Board of Directors is empowered to make a donation by passing a resolution at a Board meeting. The company is also required to make proper disclosure in the profit and loss account.

**Question 34**
M/s XYZ Ltd. was incorporated on 1st January, 2012. On 1st November, 2014 a political party approaches the company for a contribution of Rupees Ten lakhs for political purpose. Advise in respect of the following:
(i) Is the company legally authorised to give this political contribution?
(ii) Will it make any difference, if the company was in existence on 1st October, 2011?
(iii) Can the company be penalised for defiance of Rules of this regard?

**Answer**
(i) In terms of section 182 (1) of the Companies Act, 2013 the company is legally not authorized to make a political contribution unless it has been in existence for three financial years or more. Since XYZ Co. has not completed three years of existence on 2nd November 2014, it is not eligible to give political contribution.
(ii) Yes, because in that case, XYZ limited shall complete three financial years of its existence by 1.11.2014, therefore, will be eligible to give political contribution under section 182 (1) of the Companies Act, 2013. 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.
(iii) Under section 182 (4) of the Companies Act, 2013 if a company makes any contribution in contravention of the provisions of section 182, the company shall be punishable with fine which may extend to five times the amount so contributed and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to six months and with fine which may extend to five times the amount so contributed.

**Question 35**
Win Ltd. is a company incorporated 15 years ago and during the last three consecutive financial years it earned profits, of ₹ 5.00 lakhs, 8.00 lakhs and 11.00 lakhs. In order to augment its business prospects, it wants to make donations to political parties. State with reference to the provisions of the Companies Act, 2013 whether the company can make such donations and if yes to what extent. Also state which type of donation, Subscription, payment,
expenditure is regarded as contribution for political purpose.

**Answer**

According to Section 182 (1) of the Companies Act, 2013, a company, except a Government Company and a company which has been in existence for less than three financial years, can make political contributions, directly or indirectly.

Further, the contribution shall be made by a company only after passing a resolution at a meeting of the Board of Directors authorising such contributions.

Based on the provisions of the Companies Act, 2013, Win Ltd. is a company incorporated 15 years ago. In order to augment its business prospects, it wants to make donations to political parties.

Therefore, if Win Ltd. wants to make donation to political parties, it can contribute the amount without any limits.

Further, the type of donations that can be made or the payments or expenditures which will be deemed to be political contributions are laid down in sections 182 (2) which states as under:

(a) a donation or subscription or payment caused to be given by a company on its behalf or on its account 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 or made, can reasonably be regarded as likely to affect public support for a political party shall also be deemed to be contribution of the amount of such donation, subscription or payment to such person for a political purpose;

(b) The amount of expenditure incurred, directly or indirectly, by a company on an advertisement in any publication, being a publication in the nature of a souvenir, brochure, pamphlet or the like, is issued:

(i) on behalf of a political party, then it shall be deemed to be a contribution to such political party; and

(ii) not on behalf of a political party but for the advantage of a political party, it shall be deemed to be a contribution for a political purpose.

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**SECTION 183 : CONTRIBUTION TO NATIONAL DEFENCE FUNDS.**

(1) The Board of Directors of any company may contribute such amount as it thinks fit to the National Defense Fund or any other Fund approved by the Central Government for the purpose of national defense.

(2) Such contribution shall be made notwithstanding anything contained in

a) sections 180, 181 and section 182 or

b) any other provision of this Act or

c) in the memorandum, or

d) in articles or

e) any other instrument relating to the company.

(3) Every company shall disclose in its profits and loss account the total amount or amounts contributed by it to the Funds during the financial year to which the amount relates.
SECTION 184 : DISCLOSURE OF INTEREST BY DIRECTOR.

(1) **MEANING:**
- Disclosure of interest means disclosure of concern or interest by a director
- in any company or companies or bodies corporate, firms, or other association of individuals including shareholding, in such manner as may be prescribed;
- with which company is entering into a contract.

(2) **WHEN TO DISCLOSE:**
Every director shall disclose his concern or interest at the first meeting of the Board in which he participates as a director after arising of interest and thereafter at the first meeting of the Board in every financial year;

(3) **WHAT TO DISCLOSE:**
Every director of a company who is directly or indirectly, concerned or interested in a contract or arrangement entered into or proposed to be entered into must
a) **Disclose the nature of his concern** or interest at the Board meeting of the in which the contract or arrangement is discussed (by giving a notice in writing in form MBP-1) and
b) shall not participate in such meeting.

<table>
<thead>
<tr>
<th>Exceptions:</th>
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<tbody>
<tr>
<td>In case of <strong>Specified IFSC Public Company</strong> - Sub-section (2) of section 184 shall apply with the exception that interested director may participate in such meeting provided the disclosure of his interest is made by the concerned director either prior or at the meeting. - Notification Dated 4th January 2017.</td>
</tr>
<tr>
<td>In case of <strong>Private company</strong> - Section 184 (2) shall apply with the exception that the interested director may participate in such meeting after disclosure of his interest. - vide Notification G.S.R. 464(E), Notification dated 5th June, 2015.</td>
</tr>
</tbody>
</table>

(4) **CIRCUMSTANCES REQUIRING DISCLOSURE OF INTEREST:**

<table>
<thead>
<tr>
<th>Exceptions:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Whereas with respect to the companies covered under <strong>Section 8</strong> of the Companies Act, 2013, vide Notification G.S.R. 466(E), dated 5th June 2015, the 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.</td>
</tr>
</tbody>
</table>

When the agreement proposed to be entered into is:
(a) with a body corporate in which
   i) such director alone or with any other director, **holds more than 2% shareholding** of that body corporate, or
   ii) is a promoter, manager, Chief Executive Officer of that body corporate; or
(b) with a firm or other entity in which, such director is a partner, owner or member.

(5) **SUBSEQUENT ARISING OF INTEREST:**
Where a director is not so concerned or interested at the time of entering into such contract or arrangement, but he becomes concerned or interested after the contract or arrangement is entered into, then he must disclose his concern or interest at the first meeting of the Board held after he becomes so concerned or interested.

(6) **CONTRAVENTION:**
\( a)\) **CONTRACT** : A contract entered into without disclosure or with participation by a director who is concerned or interested directly or indirectly shall be voidable at the option of the company.
\( b)\) **DIRECTOR IN DEFAULT** : If a director of the company contravenes, such director shall be punishable with

\[
\text{Imprisonment upto one year}
\]
\[
\text{Fine : fifty thousand rupees upto one lakh rupees, (₹ 50,000/- -- ₹ 1,00,000/-)}
\]
\[
\text{or both.}
\]

**Question 36**

Company Y with a paid-up capital of Rs.50 lakhs entered into a contract with company Z in which a director of Y is holding equity shares of the nominal value of Rs.50,000. The director did not disclose his interest at the Board meeting under section 184 of the Companies Act, 2013. Is the director liable for his act?

**Answer**
As per section 184 (2) of the Companies Act, 2013 the disclosure of interest by directors do not apply to any contract or arrangement within two companies where any of the directors of one 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. In the present case, in case the holding of the director of Y in company Z is less than 2% \((50,000/50,00,000)*100\% = 1\%) the director is not liable.

**Question 37**
The Articles of Association of a company states that a director shall not vote in respect of a contract in which he is interested. In a resolution put up for approval of the shareholders, can a director exercise his voting right in favour of a contract in which he is interested?

**Answer**
When a director exercises his voting right as a shareholder, he is free to vote in his own best interests like any other shareholder.
A provision in the Articles of Association of a company stating that a director shall not vote in respect of a contract in which he is interested does not preclude him from voting thereon as a shareholder in the general
A shareholder may vote as he pleases even when his interests are different from or opposed to those of the company. Shareholders are not trustees for the company or for one another. However, in Cooks vs. Deeks, it was held that if directors use their position as directors to obtain for themselves the property of the company, as for example, by means of a beneficial contract, they cannot, by using their voting power as shareholders in general meeting, prevent the company from claiming the benefit of it. Hence the director can exercise his voting right at a general meeting in favour of a contract in which he is interested.

Question 38

State the circumstances in which a director of a company is required under the Companies Act, 2013 to disclose his interest in a contract or arrangement to be entered into by the company. Examine whether the validity of the contract is affected by non-disclosure of interest by the director.

Answer

Circumstances in which disclosure of Interest by director is necessary - Section 184 of the Companies Act, 2013 provides for disclosure of interest by director. According to this section whenever any 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 shall disclose the nature of his concern or interest at the meeting of the Board in which the contract or arrangement is discussed and shall not participate in such meeting.

Following are the circumstances where disclosure is necessary:

Whenever any director of the 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

(b) with a firm or other entity in which, such director is a partner, owner or member, as the case may be.

However, where any director who is not so concerned or interested at the time of entering into such contract or arrangement, he shall, if he becomes concerned or interested after the contract or arrangement is entered into, disclose his concern or interest forthwith when he becomes concerned or interested or at the first meeting of the Board held after he becomes so concerned or interested.

Validity of the contract on non-disclosure of interest: A contract or arrangement entered into by the company without disclosing or with participation by a director who is concerned or interested in any way, directly or indirectly, in the contract or arrangement, shall be voidable at the option of the company.
(1) A company shall NOT,
➢ advance any loan, including any loan represented by a book debt,
➢ directly or indirectly to or give any guarantee or provide any security in connection with any loan taken by:

a) any director of company, or of a company which is its holding company or any partner or relative of any such director; or

b) any firm in which any such director or relative is a partner.

(2) A company may advance any loan including any loan represented by a book debt, or give any guarantee or provide any security in connection with any loan taken by any person in whom any of the director of the company is interested, subject to the condition that—

(a) a special resolution is passed by the company in general meeting:

Provided that the explanatory statement to the notice for the relevant general meeting shall disclose the full particulars of the loans given, or guarantee given or security provided and the purpose for which the loan or guarantee or security is proposed to be utilised by the recipient of the loan or guarantee or security and any other relevant fact; and

(b) the loans are utilised by the borrowing company for its principal business activities.

Explanation.—For the purposes of this sub-section, the expression "any person in whom any of the director of the company is interested" means—

i) any private company of which any such director is a director or member;

ii) 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
iii) any body corporate, the Board of directors, managing director or manager, whereof is accustomed to act in accordance with the directions or instructions of the Board, or of any director or directors, of the lending company.

(3) Exceptions: This sub-section shall not apply to—

a) Any loan 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 scheme approved by the members by a special resolution;

b) A company whose ordinary course of its business is to provide loans and give guarantee and securities for the due repayment of any loan. And such company provides loans or gives guarantees or securities to or for any director/ Other specified person
   (i) in the ordinary course of its business
   AND
   (ii) 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) *A loan given by Holding Company to its WHOLLY OWNED Subsidiary Company. A guarantee given or security provided by Holding Company for loan given to its WHOLLY OWNED Subsidiary Company

d) *A guarantee given or security provided by Holding Company for loan given to it Subsidiary Company by any Bank or Financial institution.

*Provided that loans made by holding companies under clause (e) and (d) are utilized by the Subsidiary company for its principle business activities.
(4) Contravention:
   a) the company shall be punishable with
      ➢ fine not less than five lakh rupees upto 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 five lakh rupees but which may extend to twenty-five lakh rupees; and

   c) the director or the other person to whom any loan is advanced or guarantee or security is given or provided in connection with any loan taken by him or the other person, shall be punishable with
      ➢ imprisonment which may extend to six months
      ➢ or with fine not less than five lakh rupees upto twenty-five lakh rupees,
      ➢ or both.

Exemptions:

a) Vide notification G.S.R. 463(E), dated 5th June 2015, section 185 shall not apply to Government Company. Subject to:

   Prior 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.

b) Vide Notification no. G.S.R. 465(E), dated 5th June 2015, section 185 shall not apply to Nidhi companies. Subject to:

   Loan is given to director or relative in capacity of member.

   AND

   Disclosed in Annual Accounts as notes.

c) Vide Notification G.S.R 464(E), dated 5th June 2015, section 185 shall not apply to Private companies. Subject to:

   i) No investment by any other body corporate in share capital of the private company.

   ii) Borrowing from banks and Financial institutions does not exceed:
Lower of
Twice of Paid up share capital
Or
₹50 Crore.

iii) No default subsisting in such borrowings at the time of making transaction.

Question 39
Mr. X is a director of M/s ABC Ltd. He has approached M/s Housing Finance Co. Ltd. For the purpose of obtaining a loan of ₹50 lacs to be used for construction of building his residential house. The loan was sanctioned subject to the condition that M/s ABC Ltd. should provide the guarantee for repayment of loan instalments by Mr. X. Advise Mr. X.

Answer
According to section 185 of the Companies Act, 2013, no company shall, directly or indirectly, advance any loan, including any loan represented by a book debt, to any of its directors or to any other person in whom the director is interested or give any guarantee or provide any security in connection with any loan taken by him or such other person.
Thus, Mr. X is not allowed for loan of Rs. 50 Lacs by the company ABC Ltd.

Question 40
Mr. X is a director of several companies. He has approached the following companies in which he is a director for financial help to start his own personal business.
(i) Expandable Industries Ltd.
(ii) Expensive Gadgets Ltd.
(iii) Easy Finance Ltd.
The first named company has agreed to grant a loan of ₹50 lakhs. The second company also offered another loan of ₹50 lakhs. The third company has agreed to provide guarantee for the repayment of a loan sanctioned to Mr. X by a Private Bank to the tune of Rupee One crore. Advise Mr. X about the legal provisions that should be complied with under the Companies Act, 2013 and the consequences if there is a non – compliance.

Answer
According to section 185 of the Companies Act, 2013, no company shall, directly or indirectly, advance any loan, including any loan represented by a book debt, to any of its directors or to any other person in whom the director is interested or give any guarantee or provide any security in connection with any loan taken by him or such other person.
In all the three types of companies, loan or guarantee to Mr. X is not allowed. Further, If any loan is advanced or a guarantee or security is given or provided in contravention of the above provisions, the company shall be punishable with fine which shall not be less than five lakh rupees but which may extend to twenty-five lakh rupees, and the director or the other person to whom any loan is advanced or guarantee or security is given or provided in connection with any loan taken by him or the other person, shall be punishable with
imprisonment which may extend to six months or with fine which shall not be less than five lakh rupees but which may extend to twenty-five lakh rupees, or with both.

Question 41
Mr. KMP is director of XLS Ltd. He intends to construct a residential building for his own use. The cost of construction is estimated at ₹ 1.50 Crores, which Mr. KMP proposes to finance partly from his own sources to the tune of ₹ 60 lacs and the balance ₹ 90 lacs from housing loan to be obtained from a housing finance company. For the purpose of obtaining the loan, he has approached the housing finance company which has in principle agreed to grant the loan, but has put a condition. The condition put by the housing finance company is that the Company XLS Ltd. of which Mr. KMP is a director should provide the guarantee for repayment of the loan and interest as per the terms of the proposed agreement for granting the loan to Mr. KMP. You are required to advise Mr. KMP on the matter with reference to the provisions of the Companies Act, 2013.

Answer
According to section 185 of the Companies Act, 2013, no company shall, directly or indirectly, advance any loan, including any loan represented by a book debt, to any of its directors or to any other person in whom the director is interested or give any guarantee or provide any security in connection with any loan taken by him or such other person.
Thus, guarantee by Company XLS Ltd. of which Mr. KMP is a director, for repayment of the loan and interest as per the terms of the proposed agreement is not allowed.
Further, If any loan is advanced or a guarantee or security is given or provided in contravention of the above provisions, the company shall be punishable with fine which shall not be less than five lakh rupees but which may extend to twenty-five lakh rupees, and the director or the other person to whom any loan is advanced or guarantee or security is given or provided in connection with any loan taken by him or the other person, shall be not be less than five lakh rupees but which may extend to twenty-five lakh rupees, or with both.

Question 42
Mr. DRT is a director of PCS Ltd. The said company is having sufficient liquid funds and Mr. DRT is in dire need of funds. In order to mitigate the hardship of Mr. DRT the board of directors of PCS Ltd. wants to lend ₹ 5 lakhs to him and ₹ 2 lakhs to his wife. State whether such loans can be given and if so under what conditions. What would be your answer if the company PCS LTD would have been PCS Private Ltd.

Answer
Loan to Director and his relative: According to section 185 of the Companies Act, 2013, no company shall, directly or indirectly, advance any loan, including any loan represented by a book debt, to any of its directors or to any other person in whom the director is interested or give any guarantee or provide any security in connection with any loan taken by him or such other person.
Thus, in the instant case, if PCS Ltd. wants to lend ₹ 5 Lakhs to Mr. DRT who is a director in PCS Ltd. and ₹ 2 Lakhs to his wife, then it is in violation of section 185 of the Companies Act, 2013.
If PCS Ltd would have been PCS Private Ltd., Vide Notification G.S.R 464(E), dated 5th June 2015, section 185 shall not apply to a private company-
(a) In whose share capital no other body corporate has invested any money;
(b) 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
(c) Such company has no default in repayment of such borrowings subsisting at the time of making transactions under this section.

**SECTION 186 : INTERCORPORATE LOANS, INVESTMENTS ETC.**

Section 186 of the Companies Act, 2013 deals with the provisions related to Loan and Investment by Company. According to this section:

Applicability: This section is applicable on both public as well as private company.

(i) **INVESTMENT BY COMPANY * [Section 186(1)]:**
According to section 186(1), without prejudice to the provisions contained in this Act, a company shall unless otherwise prescribed, make investment through not more than 2 layers of investment companies: [Section 186(1)]
(i.e. A Company cannot make investments beyond 2 layers.)

**Exemption:**
However, the provisions of sub-section (1) shall not affect,—

(a) Acquiring of company incorporated outside India: a company from acquiring any other company incorporated in a country outside India if such other company has investment subsidiaries beyond two layers as per the laws of such country;

(b) Subsidiary from having an investment subsidiary: 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.

★ In case of Specified IFSC Public Company & Private Company - In Sub-section (1) of section 186 shall not apply. - Notification Date 4th January, 2017

(ii) **LIMITATION/RESTRICTIONS ON THE COMPANY * [Section 186(2)]:**
According to section 186 (2) of the Companies Act, 2013, there are three types of transactions:
(a) Loan
(b) Guarantee or security in connection with the loan
(c) Acquire by way of subscription, purchase or otherwise the securities of any other body corporate

No company shall give-exceeding 60% of its paid-up share capital, free reserves and securities premium account or 100% of its free reserves and securities premium account, whichever is more.

**Exemption:**
★ In case of Specified IFSC Public Company and Private Company - In Sub-sections (2) and (3) of
section 186 shall not apply if a company passes a resolution either at meeting of the Board of Directors or by circulation. - Notification Date 4th January, 2017.

<table>
<thead>
<tr>
<th>Vide General Circular No, 04/2015, dated 10/3/2015 clarification has been issued on the applicability of provisions of section 186 of the Companies Act, 2013 relating to grant of loans and advances by Companies to their employees.</th>
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<tr>
<td>It has been 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 of the Companies Act, 2013. 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.</td>
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It can be interpreted that company can do transactions given in headings 1, 2 or 3 upto 60% of paid up share capital, free reserves and securities premium account or 100% of its free reserves and securities premium account (whichever is more) and restrictions apply only when such transactions exceeds the limits.

(iii) PRIOR APPROVAL FOR EXCEEDING LIMIT [Section 186(3)]:

Prior approval by means of a special resolution passed at a general meeting shall be necessary where the giving of any loan or guarantee or providing any security or the acquisition exceeds the limits specified above.

<table>
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<tr>
<th>Exemption:</th>
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<tr>
<td>According to the Rule 11 of the Companies (Meetings of Board and its Powers) Rules, 2014, 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 sub-section (3) of section 186 shall not apply. Provided that the company shall disclose the details of such loans or guarantee or security or acquisition in the financial statement as provided under sub-section (4) of section 186.</td>
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<th>As per the Rule 13 of the Companies (Meetings of Board and its Powers) Rules, 2014, also provides that:</th>
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<td>(a) 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, 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. Explanation.- For the purpose of this rule, it is clarified that it would sufficient compliance if such special resolution is passed within one year from the date of notification of this section.</td>
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(b) A resolution passed at a general meeting in terms of sub-section (3) of section 186 to give any loan or guarantee or investment or providing any security or the acquisition under sub section (2) of
section 186 shall specify the total amount up to which the Board of Directors are authorised to give such loan or guarantee, to provide such security or make such acquisition:
Provided, that the company shall disclose to the members in the financial statement the full particulars in accordance with the provision of sub-section (4) of section 186.

(iv) **DISCLOSURE TO MEMBERS [Section 186(4)]:**
Company shall disclose to the members in the financial statement 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 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.
However, prior approval of a public financial institution 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) and there is no default in repayment of loan instalments or payment of interest thereon as per the terms and conditions of such loan to the public financial institution.

★ In case of Specified IFSC Public & Private Company - In Sub-section (5) of section 186 after the proviso, the following proviso shall be inserted -
“Provided that the Board can exercise powers under this sub-section by means of resolutions passed at meetings of the Board of Directors or through resolutions passed by circulation.” - Notification Date 4th January, 2017.]

(vi) **RESTRICTION ON THE INTER-CORPORATE LOANS/DEPOSITS [Section 186 (6)]:**
Further, no company, which is registered under section 12 of the Securities and Exchange Board of India Act, 1992 and covered under such class or classes of companies as may be prescribed, shall take inter-
corporate loan or deposits exceeding the prescribed limit and such company shall furnish in its financial statement the details of the loan or deposits.

According to Rule 11(3) to the Companies (Meetings of Board and its Powers) Rules, 2014, no company registered under section 12 of the Securities and Exchange Board of India Act, 1992 and also 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 take any inter-corporate loan or deposits, in excess of the limits specified under the regulations applicable to such company, pursuant to which it has obtained certificate of registration from the Securities and Exchange Board
(vii) **RATE OF INTEREST ON LOAN [Section 186 (7)]:**
A loan under this section shall not be given at a rate of interest lower than the prevailing yield of one year, 3 year, 5 year or 10 year Government Security closest to the tenor of the loan. [Section 186 (7)]

Vide General circular no. 06/2015 dated 9th April, 2015 ministry 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 this section of the Companies Act, 2013.

(viii) **NO LOAN TILL DEFAULT IS SUBSISTING [Section 186 (8)]:**
No company which is in default in the repayment of any deposits accepted before or after the commencement of this Act or in payment of interest thereon, shall give any loan or give any guarantee or provide any security or make an acquisition till such default is subsisting.

(ix) **MAINTENANCE OF REGISTER [Section 186 (9)]:**
Every company giving loan or giving a guarantee or providing security or making an acquisition under this section shall keep a register which shall contain such particulars and shall be maintained in such manner as prescribed In Rule 12 and MBP 2 of the Companies (Meetings of Board and its Powers) Rules, 2014.

According to Rule 12 of the Companies (Meetings of Board and its Powers) Rules, 2014:
(a) Every company giving loan or giving guarantee or providing security or making an acquisition of securities shall, from the date of its incorporation, maintain a register in Form MBP 2 and enter therein separately, the particulars of loans and guarantees given, securities provided and acquisitions made as aforesaid.

(b) The entries in the register shall be made chronologically in respect of each such transaction within 7 days of making such loan or giving guarantee or providing security or making acquisition
(c) The register shall be kept at the registered office of the company and the register shall be preserved permanently and shall be kept in the custody of the company secretary of the company or any other person authorised by the Board for the purpose.
(d) The entries in the register (either manual or electronic) shall be authenticated by the company secretary of the company or by any other person authorised by the Board for the purpose.
(e) The register can be maintained either manually or in electronic mode.
(f) The extracts from such register maintained may be furnished to any member of the company on payment of such fee as may be prescribed in the Articles of the company which shall not exceed 10 rupees for each page.

(x) **REGISTER TO BE KEPT AT REGISTERED OFFICE [Section 186 (10)]:**
(a) This register shall be kept at the registered office of the company.
(b) It shall be open to inspection at such office and extracts may be taken therefrom by any member, and copies thereof may be furnished to any member of the company on payment of such fees as prescribed in Rule 12.
(xi) **NON-APPLICABILITY OF SECTION 186 [Section 186 (11)]:**
Nothing contained in section 186, except sub-section (1) of section 186, shall apply—
(a) to a loan made, guarantee given or security provided by a banking company or an insurance company or a housing finance company in the ordinary course of its business or a company engaged in the business of financing of companies or of providing infrastructural facilities;

(b) to any acquisition—
(1) made by a non-banking financial company registered under Chapter IIIB of the Reserve Bank of India Act, 1934 and whose principal business is acquisition of securities:
   Provided that exemption to non-banking financial company shall be in respect of its investment and lending activities;
(2) made by a company whose principal business is the acquisition of securities;
(3) of shares allotted in pursuance of section 62(1)(a) [Section 186 (11)]
(4) made by the banking company or an insurance company or a housing finance company, making acquisition of securities in the ordinary course of its business.

(xii) **POWER OF CENTRAL GOVERNMENT TO MAKE RULES [Section 186 (12)]:**
The Central Government may make rules for the purposes of this section.

(xiii) **PENALTY [Section 186 (13)]:**
If a company contravenes the provisions of section 186, the company shall be punishable with fine which shall not be less than 25,000 rupees but which may extend to 5 lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to two years and with fine which shall not be less than 25,000 rupees but which may extend to 1,00,000 rupees.

For the purposes of section 186,
(a) the expression “investment company” means a company whose principal business is the acquisition of shares, debentures or other securities;
(b) the expression “infrastructure facilities” means the facilities specified in Schedule VI.

<table>
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<tr>
<th>Exemptions</th>
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<tbody>
<tr>
<td><strong>In case of Government Company - Section 186 shall not apply to:</strong></td>
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<tr>
<td>(a) a Government company engaged in defence production;</td>
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<tr>
<td>(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</td>
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</tbody>
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guarantee or providing any security or making any investment under the section. - Notification dated 5th June, 2015.

Question 43
Amar Textiles Ltd. is a company engaged in the manufacture of fabrics. The company has investments in shares of other bodies corporate including 70% shares in Amar Cotton Company Ltd. and it has also advanced loans to other bodies corporate. The aggregate of all the investments made and loans granted by Amar Textiles Ltd. exceeds 60% of its paid up share capital and free reserves and also exceeds 100% of its free reserves. In course of its business requirements, Amar Textiles Ltd. has obtained a term loan from Industrial Development Bank of India which is still subsisting. Now the company wants to increase its holding from 70% to 80% of the equity share capital in Amar Cotton Company Ltd. by purchase of additional 10% shares from other existing shareholders. State the legal requirements to be complied with by Amar Textiles Ltd. under the provisions of the Companies Act, 2013 to give effect to the above proposal.

Answer
Amar Cotton Co. Ltd. is not a wholly-owned subsidiary of Amar Textiles Ltd.

1. According to section 186(2) of the Companies Act, 2013, no company shall directly or indirectly —
   (a) give any loan to any person or other body corporate;
   (b) give any guarantee or provide security in connection with a loan to any other body corporate or person; and
   (c) acquire by way of subscription, purchase or otherwise, the securities of any other body corporate, exceeding 60% of its paid-up share capital, free reserves and securities premium account or 100% of its free reserves and securities premium account, whichever is more.
   As the aggregate of the investments in shares and loans granted to other bodies corporate exceeds 60% of the paid-up share capital and free reserves and also 100% of the free reserves, it exceeds the limit under section 186(2) of the Companies Act, 2013. It is therefore, necessary for Amar Textiles Ltd., to pass a special resolution of the members at a duly convened General Meeting before increasing its holding from 70% to 80%.

2. The notice of special resolution must be accompanied by an explanatory statement and must include full particulars of the investment proposed to be made along with the purpose of such investment in compliance with section 186(4) of the Act.

3. According to section 186(5) of the Companies Act, 2013, no investment shall be made or loan or guarantee or security given by the company unless the resolution sanctioning it is passed at a meeting of the Board with the consent of all the directors present at the meeting and the prior approval of the public financial institution concerned where any term loan is subsisting, is obtained:
   However, prior approval of a public financial institution 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 186(2), and there is no default in repayment of loan instalments or payment of interest thereon as per the terms and conditions of such loan to the public financial institution.
   In the present case, Amar Textiles Ltd., had obtained a term loan from Industrial Development Bank of India (IDBI) which is not a public financial institution within the meaning under Section 2 (72) of the Companies
Act, 2013 and therefore the provisions of Section 186 (5) are not attracted even if such loan is still subsisting. The company is not required to obtain prior approval of IDBI for making any further investment.

4. Further, as required by provisions of Section 186 (5), the investment proposal must be passed at the Board meeting by a unanimous decision of all the directors present at the meeting.

5. The company must enter the prescribed particulars of investment in a register of investment required to be maintained under section 186(9) of the Act.

SECTION 187 : INVESTMENTS OF COMPANY TO BE HELD IN ITS OWN NAME.

(1) All investments held by a company must be in its own name.

(2) But the company may hold any shares in its subsidiary company in the name of any nominee or nominees of the company, if it is necessary to do so, to ensure that the number of members of the subsidiary company is not reduced below the statutory limit.

(3) Exception— In the following cases Investments may be held in a name other than company’s own name.
   a) Depositing with a bank, being the bankers of the company, any shares or securities for the collection of any dividend or interest payable thereon; or

   b) Depositing with, or transferring to, or holding in the name of, the state bank of india or a scheduled bank, being the bankers of the company, shares or securities, in order to facilitate the transfer thereof.
   *Provided that if transfer does not take place within a period of six months from the date on which the shares or securities are transferred by the company to the state bank of india, the company shall, as soon as practicable after the expiry of that period, have the shares or securities re-transferred to it from the state bank of india in its own name; or

   c) Depositing with, or transferring 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) Holding investments in the name of a depository when such investments are in the form of securities held by the company as a beneficial owner.

(4) Where in pursuance of point (d) of (3), any shares or securities in which investments have been made by a company are not held by it in its own name, the company must maintain a register which shall contain such particulars as may be prescribed and such register shall be open to inspection by any member or debenture-holder of the company without any charge during business hours subject to such reasonable restrictions as the company may by its articles or in general meeting impose.

(5) If a company contravenes the provisions of this section, the company shall be punishable
   fine : twenty-five thousand rupees upto twenty-five lakh rupees ( ₹ 25,000 - ₹ 25,00,000)
and every officer of the company who is in default shall be punishable
imprisonment: upto 6 months or
fine: twenty-five thousand rupees upto one lakh rupees, (₹ 25,000 - ₹ 1,00,000)
or
both.

According to Rule 14 of the Companies (Meetings of Board and its Powers) Rules, 2014,
a) Every company shall, from the date of its registration, maintain a register in Form MBP3 and
enter therein, chronologically, the particulars of investments in shares or other securities
beneficially held by the company but which are not held in its own name and the company shall
also record the reasons for not holding the investments in its own name and the relationship or
contract under which the investment is held in the name of any other person.
b) The company shall also record whether such investments are held in a third party’s name for the
time being or otherwise.
c) The register shall be maintained at the registered office of the company. The register shall be
preserved permanently and shall be kept in the custody of the company secretary of the company
or if there is no company secretary, any director or any other officer authorised by the Board for
the purpose.
d) 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.

SECTION 188: RELATED PARTY TRANSACTIONS.

(1) Related party transaction: Any contract or arrangement with a related party with respect to—
a) sale, purchase or supply of any goods or materials;
b) selling or otherwise disposing of, or buying, property of any kind;
c) appointment of any agent for purchase or sale of goods, materials, services or property;
d) leasing of property of any kind;
e) availing or rendering of any services;
f) such related party's appointment to any office or place of profit in the company, its
subsidiary company or associate company; and
g) underwriting the subscription of any securities or derivatives thereof, of the company:

(2) Approval of the Board of Directors by an ordinary resolution at a Board meeting should be taken.

(3) In the case of a company having Transactions exceeding prescribed sums, according to Rule
15(3) of the Companies (Meetings of Board and its Powers) Rules, 2014,
Prior approval of the company by an ordinary resolution will be mandatory.
In case of wholly owned subsidiary, the resolution is passed by the holding company shall be sufficient for the purpose of entering into the transaction between the wholly owned subsidiary and the holding company.

A member of the company who is also a related party shall not vote on such ordinary resolution.

The MCA vide General Circular No. 30/2014 dated 17th July, 2014 has clarified the scope of second proviso to section 188(1). *The second proviso to subsection (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. It is 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. According to Rule 15(2) of the Companies (Meetings of Board and its Powers) Rules, 2014, where any director is interested in any contract or arrangement with a related party, such director shall not be present at the meeting during discussions on the subject matter of the resolution relating to such contract or arrangement.

| Exemptions from rule of “Related party member not to vote”:
| This second proviso to section 188(1) shall not apply to **private company** - Notification dated 5th June, 2015
| In case of **Specified IFSC Public Company** - Second proviso to sub section (1) of section 188 shall not apply. - Notification Date 4th January, 2017

| Exemption from rules of “Shareholders approval” & “Related party member not to vote”:
| Vide Notification G.S.R. 463(E) dated 5th June 2015, 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 administratively in charge of the company, or as the case may be, the state Government before entering into such contract or arrangement.

{* Not Applicable if :
(a) Transaction between 2 Government companies. Or
(b) Transaction by an Unlisted Government company, with approval of Government.}

| Exemption from “Related party member not to vote” (#Amendment)
Provided also that 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

| Exemption from shareholders approval:
Passing of resolution is not necessitated: Provided also that the requirement of passing resolution
under first proviso shall not be applicable for transactions entered into between a holding company and its wholly owned subsidiary whose accounts are consolidated with such holding company and placed before the shareholders at the general meeting for approval.

(4) According to The Companies (Meeting of Board and its Powers) Rules, 2014 Members resolution shall be mandatory in the following cases. Where the transaction to be entered into:

(A) when conditions (a) to (e) of S2ALSA U falls under the following criteria:

(i) sale, purchase or supply of any goods or materials either directly or through appointment of any agent, where value of transaction \( \text{amounting to} \):

\[
10\% \text{ of the TURNOVER of the Company} \\
\text{or} \\
\text{₹ } 100 \text{ Crore} \\
\text{Whichever is Lower.}
\]

(ii) selling or otherwise disposing of, or buying, property of any kind, either directly or through appointment of any agent, where value of transaction \( \text{amounting to} \):

\[
10\% \text{ of the NETWORTH of the Company} \\
\text{or} \\
\text{₹ } 100 \text{ Crore} \\
\text{Whichever is Lower.}
\]

(iii) leasing of property of any kind where value of transaction \( \text{amounting to} \):

\[
10\% \text{ of the NETWORTH of the Company} \\
\text{or} \\
10\% \text{ of the TURNOVER of the Company} \\
\text{or} \\
\text{₹ } 100 \text{ Crore} \\
\text{Whichever is Lower.}
\]

(iv) Availing or rendering of any services, either directly or through appointment of any agent, where value of transaction \( \text{amounting to} \):

\[
10\% \text{ of the TURNOVER of the Company} \\
\text{or} \\
\text{₹ } 50 \text{ Crore} \\
\text{Whichever is Lower.}
\]

(B) is for appointment to any office or place of profit in the company, its subsidiary company or associate company at a monthly remuneration exceeding ₹ 2.5 lakh.

(C) is for remuneration for underwriting the subscription of any securities or derivatives thereof, of the company exceeding 1% of the Networth.
(5) **Exception:**

Any transactions entered into by the company in its ordinary course of business and
➢ Any transactions entered into by the company at arm’s length basis.

(6) Every RPT entered shall be disclosed in the Board’s report along with the justification for entering into such contract or arrangement.

(7) **Contravention:**

*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.*

(8) The company can proceed against a director or any other employee who had entered into such contract or arrangement in contravention of the provisions of this section for recovery of any loss sustained by it as a result of such contract or arrangement.

(9) **Any director or any other employee** of a company, who had entered into or authorized the contract or arrangement in violation of the provisions of this section shall,—

(i) In case of listed company, be punishable with

- Imprisonment upto one year or
- Fine : Twenty-five thousand rupees upto Five lakh rupees, (₹25,000 – ₹5,00,000) or
- Both;

AND

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(ii) In case of any other company, be punishable with
Fine : Twenty-five thousand rupees upto Five lakh rupees. ( ₹ 25,000 – ₹ 5,00,000)

SECTION 189 : REGISTER OF CONTRACTS OR ARRANGEMENTS IN WHICH
DIRECTORS ARE INTERESTED.

(1) Every company shall keep one or more registers giving separately such particulars as may be
prescribed of all contracts or arrangements under section 184 or section 188, 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.

According to Rule 16 of the Companies (Meetings of Board and its Powers) Rules, 2014,
every company shall maintain one or more registers in Form MBP 4, and contain such
particulars as required therein.

(2) Every director or key managerial personnel shall, within thirty days of his appointment, disclose
to the company the particulars specified in sub-section (1) of section 184 relating to his concern
or interest in the other associations which are required to be included in the register under that
sub-section or such other information relating to himself as may be prescribed.

(3) The register shall be kept at the registered office of the company and it shall be open for
inspection at such office during business hours and copies may be taken as may be required by
any member on payment of such fees as may be prescribed.

According to the Companies (Meetings of Board and its Powers) Rules, 2014, such fee will
be as provided in the articles of the company, subject to the maximum of ₹10 for each page.

(4) The register to be kept under this section shall also be produced at the commencement of every
annual general meeting of the company and shall remain open and accessible during the
continuance of the meeting to any person having the right to attend the meeting.

(5) Exception: Any contract or arrangement—

(a) for the sale, purchase or supply of any goods, materials or services if the value of such
goods and materials or services does not exceed five lakh rupees in the aggregate in any year;
or

(b) by a banking company for the collection of bills in the ordinary course of its business.

(6) Every director who fails to comply with the provisions shall be liable to a penalty of twenty-five
thousand rupees.

SECTION 190 : CONTRACT OF EMPLOYMENT WITH MANAGING OR WHOLE TIME
DIRECTORS.

(1) Every company shall keep at its registered office,—
(a) a copy of the contract of service with a managing or whole-time director where a contract is in writing; or
(b) where such a contract is not in writing, a written memorandum setting out its terms.

(2) The copies of the contract or the memorandum shall be open to inspection by any member of the company without payment of fee.

(3) If any default is made, the company shall be liable to a penalty of twenty-five thousand rupees and every officer of the company who is in default shall be liable to a penalty of five thousand rupees for each default.

(4) The provisions of this section shall not apply to a private company.

**SECTION 191 : COMPENSATION FOR LOSS OF OFFICE IN CONNECTION WITH TRANSFER OF UNDERTAKING, PROPERTY OR SHARES.**

(1) A director of a company shall not receive any payment by way of compensation for loss of office or as consideration for retirement from office, or in connection with such loss or retirement in case of:
(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—
   (1) an offer made to the general body of shareholders.
   (2) 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;
   (3) 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
   (4) any other offer which is conditional on acceptance to a given extent, unless
   ➔ particulars and the amount with respect to the payment proposed to be made, have been disclosed to the members of the company and
   ➔ the proposal has been approved by the company in general meeting.

(2) Exception: However, nothing in sub-section (1) shall affect any payment made by a company to a managing director or whole-time director 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 subject to limits or priorities set out u/s 202.

(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.

(4) If a director receives payment of any amount in contravention of (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.

(5) Contravention: If a director of the company contravenes the provisions of this section, such director shall be punishable with a fine of flat one lakh rupees.

(6) According to Rule 17 of The Companies (Meeting of Board and its Powers) Rules, 2014:
   (a) Particulars to be disclosed to members for taking approval:
      (i) Name of Director.
      (ii) Amount proposed to be paid.
      (iii) Event due to which compensation became payable.
      (iv) Date of Board meeting.
      (v) Basis for amount determined.
      (vi) Reason for justification of payment.
      (vii) Manner of payment.
      (viii) Sources of payment.
      (ix) Other relevant particulars.
   (b) Compensation for loss of office shall not be paid if:
      (i) The company has defaulted in repayment of Public deposits or Interest thereon.
      (ii) The company has defaulted in Redemption of Debentures or payment of Interest thereon.
      (iii) The company has defaulted in repayment of any liability, secured or unsecured payable to bank or Public financial Institution or any other financial Institution.
      (iv) The company has defaulted in payment of dues towards Taxes and duties by whatever name called, payable to CG, SG, Local authority or Statutory authority.
      (v) There are outstanding dues payable to Workmen and employees of the company.
      (vi) The company has not paid dividend on preference shares or has not redeemed preference shares on due date.

SECTION 192 : RESTRICTION ON NON CASH TRANSACTION INVOLVING DIRECTORS.

(1) Any 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,
Shall be done only after prior approval by a resolution of the company in general meeting

AND

If the director 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.

(2) The notice for approval of the resolution by the company or holding company in general meeting shall include the particulars of the arrangement along with the value of the assets involved in such arrangement duly calculated by a registered valuer.

(3) Any arrangement entered into by a company or its holding company in contravention of the provisions of this section shall be voidable at the instance of the company unless—

(a) 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) any rights are acquired bona fide for value and without notice of the contravention of the provisions of this section by any other person.

**Question 44**

In what way does the Companies Act, 2013 restricts the non-cash transactions involving directors of public limited company? Explain.

**Answer**

Restrictions on non-cash transactions involving Directors: Section 192 of the Companies Act, 2013 provides for restrictions on non-cash transactions involving directors. According to the provision,

(i) 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, unless prior approval for such arrangement is accorded by a resolution of the company in general meeting and if 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.

(ii) The notice for approval of the resolution by the company or holding company in general meeting shall include the particulars of the arrangement along with the value of the assets involved in such arrangement duly calculated by a registered valuer.

(iii) Any arrangement entered into by a company or its holding company in contravention of the provisions of this section shall be voidable at the instance of the company unless—

(a) 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
Section 193 : Contract by one person company.

(1) Where One Person Company limited by shares or by guarantee enters into a contract with the sole member of the company who is also the director of the company, the company shall, unless the contract is in writing, 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:
   Exception : Contracts entered into by the company in the ordinary course of its business.

(2) The company shall inform the Registrar about every contract entered into by the company and recorded in the minutes of the meeting of its Board of Directors within a period of fifteen days of the date of approval by the Board of Directors.

SECTION 194 : PROHIBITION ON FORWARD DEALINGS IN SECURITIES OF COMPANY BY DIRECTOR OR KEY MANAGERIAL PERSONNEL.

OMITTED.

SECTION 195 : PROHIBITION ON INSIDER TRADING OF SECURITIES.

OMITTED.