CS Makarand Joshi

CORPORATE LAWS

Case Law Update

1. Companies Act

***Puthenpurakal Properties Private Ltd. (Petitioner)* v. *UNION OF INDIA* (1st Respondent) and Registrar of Companies (2nd Respondent) Judgement dated 2nd March, 2021, Kerala High Court**

Facts of the case:

cPetitioners had **part time Company Secretaries and Auditors** to **look after the affairs of their Companies** and petitioner did not have whole time CS

- Petitioner filed a **writ petition seeking to direct** the respondents **to permit** the petitioners **to file e-form ACTIVE (INC-22A) without** insisting on **appointment** of **a whole Time Company Secretary(CS)**
- Further sought to **declare that the restriction imposed** in filing **e-form ACTIVE (INC-22A)** with regards to **non-compliance of Sec. 203** of whole Time Company Secretary **or Rule 8A** of Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014 **is arbitrary and illegal**
- When this writ petition came for admission, an **interim order was passed by the Kerala High court permitting the petitioners to file e-form** ACTIVE, INC-22A, PAS-3 and DIR-12 **without insisting** on **appointment of a whole time CS provisionally**.

Arguments on behalf of Petitioner

- Petitioner submitted that MCA by exercising **powers u/s 469** of Companies Act, 2013 **amended Companies (Incorporation) Rules**, 2014 by notification dated 21.02.2019.
- As per new added **rule 25A** every Company incorporated **on or before 31.12.2017** shall **file** the particulars of the Company and its registered office in **e-form ACTIVE** on or **before 25.04.2019.**
- Further stated that **MCA is not accepting e-form** ACTIVE submitted by petitioners for the **reason** that **paid up capital is more than 5 crore** and still the petitioner has **not appointed whole time CS.**

- Petitioners have **part time Company Secretaries and Auditors** to properly **look after the affairs of their Companies** and for the last so many years, they have been functioning well within the provisions of the act without giving any room for initiating any penalty proceedings
- Therefore they **should not be forced to appoint a whole time CS** and should be permitted to file e-form ACTIVE without insisting on the appointment of a whole time Company Secretary

Arguments on behalf of Respondent

- Learned Central Government counsel appearing on behalf of respondent argued that:
- As per interim order, the petitioners have been permitted to file e-form ACTIVE without insisting on the appointment of a whole-time Company Secretary, on a provisional basis
- As per **existing rules**, **petitioners are bound to appoint whole time CS**, as paid up capital is more than 5 crores, the petitioner **cannot be granted any exemption** from the rules.
- Non-appointment of CS by petitioners company is an **offence u/s 383A (1A) vide** Companies Amendment Act, 1988 w.e.f. 01.12.1988 and also stated about the penal provisions then as per Sec. 383A of Companies Act, 1956 and also offence u/s 203 read with Rule 8A of Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014

Held

- After hearing learned counsel for the petitioners and Learned Central Government Counsel appearing for the respondent, court held that:
- As things stand now, the petitioners have been permitted to file e-form ACTIVE, INC-22A without insisting the appointment of a whole-time Company Secretary, on a provisional basis.
- Further referred penal provision given in Section 203(5)
- Further stated that it is evident that the petitioners Company has not adhered to the provisions of Companies Act, especially Sec. 203 thereof, in such circumstances the respondents are empowered to proceed against the petitioner-companies in accordance with the law.
- Writ petitions are disposed of granting liberty to the respondents to proceed against the petitioner-companies for violation of Sec. 203 of Companies Act, 2013
- Interim orders passed in these writ-petitions shall not be taken as pronouncements on merits on the legality of section 203 of Companies Act, 2013 or rule 8A of Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014.

2. SEBI

Ruling of Presiding Officer – Securities Appellate Tribunal ('SAT')

Name of the Case: Anil Mittal…. Appellant v. Securities and Exchange Board of India ('SEBI') ….Respondent

Facts of the case:

1. On June 22, 2017 Indiabulls Real Estate Ltd ('IBREL') informed Bombay Stock Exchange ('BSE') at 12:15 PM and

National Stock Exchange ('NSE') on 12:17 PM regarding the sale of its 3.3 Crore shares by its promoter entity **IBREL IBL Scheme Trust** ("**Trust**") of which IBREL was the sole beneficiary. Post this announcement on June 22, 2017, the price of the scrip fell from Rs.204.70 at 12:15:06 to Rs.192.00 on the same day, thereby registering a fall of 6.20%. As compared to the previous day closing price, the price of IBREL shares fell by 9.80% on NSE and 9.76% on BSE which was a significant fall. Thus, the announcement made by IBREL on June 22, 2017 with respect to sale of shares of the IBREL by Trust was considered to have materially impacted the price of the shares and hence was considered to be an Unpublished Price Sensitive Information **("UPSI")** in terms of Regulation 2(1)(n) of SEBI (Prohibition of Insider Trading) Regulations, 2015 ["SEBI PIT"]. This Trust was a part of Promoter and Promoter Group as at quarter ended March 2017. The Trust was holding 4.25 Crore shares (8.88%) of IBREL as of the quarter ended March 2017.

2. SEBI stated that UPSI came into existence on June 8, 2017 when a meeting by Operations Committee was held to authorise to dispose of 4.25 Crore equity shares of IBREL in one or more tranches at such time(s) and at such price(s) as may be considered appropriate by the Trustees of the Trust. This UPSI remained unpublished till June 22, 2017. Thus the period of UPSI was taken to be the period from June 8, 2017 to June 22, 2017 ['UPSI Period']. Trust had sought pre-clearance from IBREL on June 15, 2017 to sell 3.3 crore shares.

3. On further investigation SEBI observed that the Chief Financial Officer ("CFO") of IBREL ("**Appellant**") at that point of time had traded during the UPSI period. Appellant had sold 10,000 shares of IBREL on June 12, 2017. It was also found that Appellant had also attended the meeting of Operations Committee as 'Invitee' on June 8, 2017. Appellant was CFO of the IBREL for a continuous period of more than six months prior to the commencement of the UPSI so he was considered as a connected person and Insider as per Regulation 2(e)(i) of SEBI PIT.

4. So Adjudicating Officer ('AO') vide its order dt: July 10, 2020 levied a penalty of Rs 10 lakh on Appellant for violation of Regulation 4(1) of SEBI PIT read with Section 12A (d) and (e) of the Securities and Exchange Board of India Act 1993. This penalty was imposed under Section 15G(i) of the Securities and Exchange Board of India Act, 1993. This order of SEBI AO is challenged by Appellant before SAT vide its appeal no. 576 of 2020.

Charges levied

Violation of Regulation 4(1) SEBI PIT read with section 12A (d) and (e) of the Securities and Exchange Board of India Act, 1992.

Arguments made by Appellant

1. **No UPSI:** Learned Counsel on behalf of Appellant argued that there was no UPSI on the date of the sale made by the appellant. The UPSI came into existence only on June 15, 2017 when the Trust sought pre-clearance for sale. Learned Counsel further argued that Compensation Committee had permitted the Trust to sell the shares. The actual

decision of selling shares was that of Trust. Appellant was not privy to the decision taken by the Trust regarding the timing of the sale of shares of IBREL.

2. **Pre-clearance was taken:** Learned Counsel submitted that as a matter of abundant caution the Appellant had also taken pre-clearance from the Compliance Officer for his sale of 10,000 shares. Learned Counsel further argued that Appellant needed money for meeting his tax obligations. He further argued that the Trust itself holds that there was no UPSI in question.

Arguments made by Respondent

1. **No UPSI:** Learned Senior Counsel on behalf of Respondent stated that Appellant had attended the meeting of the Operations Committee on June 8, 2017 and was privy to the decision therein, authorising the Trust to sell its holding of 8.88% shares in IBREL and to remit the proceeds to IBREL. Further, Learned Senior Counsel for Respondent stated that argument by Appellant that authorising the Trust to sell its holding was not UPSI, as it was just permission given to Trust to sell shares and he was not privy to decision taken by Trust regarding the timing etc. of the sale of those shares, does not hold merit as actual disclosure by IBREL regarding the said sale transactions on June 22, 2017 resulted in an almost 10% decline in the price of IBREL shares. Therefore it is clear that UPSI came into existence from June 08, 2017 and remained UPSI till June 22, 2017. Learned Senior Counsel further submitted that Appellant sold the shares on June 12, 2017 when the UPSI was in existence. Hence it can be seen that Appellant being an "insider", was privy to the UPSI and sold the shares during UPSI period. Learned Senior Counsel further submitted that as an insider he could not have traded in the shares during UPSI Period.

2. **Pre-Clearance:** Learned Senior Counsel contended that being the CFO of IBREL the Appellant was a "designated person" who could not have sought pre-clearance for trading in the securities of the company during any UPSI Period. UPSI was from June 08, 2017 till June 22, 2017 and the appellant sold the shares on June 12, 2017. As an Insider and being privy to UPSI he should not have traded in shares by taking pre-clearance. So the Appellant not only sought pre-clearance but sought it by making false declarations that he was not privy to any UPSI.

Held by SAT

Appeal Dismissed and penalty of ₹ 10 lakh imposed by Respondent upheld for following reasons:

1. SAT held that there is no merit in the contention of the Appellant that no UPSI existed at the time of sale of 10,000 shares of IBREL on 12th June 2017 and UPSI came into existence only on June 15, 2017 when the Trust sought pre-clearance, which Appellant was not aware because the Trust was created only for the benefit of IBREL and the Compensations Committee could direct the Trust to sell its entire shareholding in IBREL and to remit the proceeds to IBREL. SAT further held that Trust was under obligation to operate under the directions given by a competent authority set up by IBREL and, therefore, though a separate legal entity it was not free to take

decisions relating to its holding of IBREL shares.

2. SAT further noted that Appellant's contention that being a part of the Committee meeting which authorised the transaction of the shares held by the Trust itself was not a UPSI does not have any merit as the Trust was holding 8.88% shares of IBREL and any decision relating to its divestment would materially impact the price of IBREL shares. SAT further stated that the Appellant was a designated person and was having UPSI, in spite of this he sought pre-clearance, gave wrong declaration and sold the shares. SAT further stated that though a caveat is given for compelling circumstances under Regulation 4(1) of SEBI PIT the Appellant's submission does not fall under such exemptions.

3. SAT further held that there is no merit in the contention of the Appellant that he sold the shares not on the basis of UPSI but for meeting his tax obligations. SAT stated that it is an admitted position that on May 19, 2017 the appellant sought pre-clearance for the sale of his entire shareholding of 15,000 shares of IBREL but for his own reasons he sold only 5,000 shares and waited till June 12, 2017 for disposing off the remaining 10,000 shares. Further, it is a widely known and admitted position that tax obligations had to be met on or before July 31 of that year and there was sufficient time available to the appellant. Further SAT noted that it is also on record that the tax obligation was not to the tune of the full amount of the sale proceeds. Appellant had to borrow ₹ 25 lakhs for the purpose of paying tax. Therefore, the requirement of funds as the reasons submitted by the appellant, in the facts of this case does not have any merit.

Cases referred

Appellant

1. *Arun Jain in the matter of Polaris Software Lab Limited [Order dated WTM/GM/EFD/109/2017-18],*
2. *Rajiv Gandhi vs. SEBI [Order dated May 9, 2008 in Appeal No. 50 of 2007],*
3. *Chandrakala vs. SEBI [Order dated January 31, 2012 in Appeal No. 209 of 2011],*
4. *Rakesh Agarwal vs. Securities and Exchange Board of India [MANU/SB/0208/2003],*
5. *In Re: Polaris Software Lab Limited and Ors. [MANU/SB/0141/2018],*
6. *Dilip Pendse vs. SEBI [Order dated November 19, 2009 in Appeal No. 80 of 2009],*
7. *Utsav Pathak [AO Order dated August 30, 2019],*
8. *Samir C Arora vs. SEBI [Order dated October 15, 2004] and*
9. *Udayant Malhoutra [WTM Order dated December 18, 2020]*

Respondent

1. *Shri B. Rama Ramalinga Raju vs. SEBI (Appeal No. 286 of 2014 decided on 12.05.2017),*
2. *Shruti Vora vs. SEBI (A. L. No. 28 of 2020 decided on 12.02.2020 and*
3. *Anant R. Sathe vs. SEBI (Appeal No. 150 of 2020 decided on 17.07.2020).*

3. IBC

In the matter of Mr. Manmohan Jhawar, Insolvency Professional ("IP") – order dated 6 November, 2020 passed by the Disciplinary Committee (DC) of Insolvency and Bankruptcy Board of India (IBBI)

Facts of the Case

- In exercise of power under section 218 of the Insolvency and Bankruptcy Code, 2016 ("**Code/IBC**"), the IBBI issued a Show Cause Notice (SCN) on 22 June, 2020 to Mr. Jhawar - IP based on findings of Inspection Authority (IA) in respect of his role as an interim resolution professional ("**IRP**") and / or resolution professional ("**RP**") in corporate insolvency resolution process ("**CIRP**") of M/s. Hahnemann Housing and Development Private Limited ("**Corporate Debtor**") which commenced vide order dated 26 April, 2018 passed by National Company Law Tribunal ("**NCLT**") Kolkata Bench.
- The SCN alleged the following contraventions:
  - — One of the primary duties of IP as laid down u/s 18 and u/s 25 of the Code includes taking control and custody of assets of the Corporate Debtor. The NCLT, in its order dated 29 October, 2018 observed that the IP failed to make efforts to take effective control and custody of seven properties (agricultural lands) of the Corporate Debtor in respect of which title deeds were also handed over by the promoters.
  - — IP failed to take any action under the relevant provisions of the Code even after NCLT recommended that appropriate action under the Code may be initiated against the promoters and directors for not providing relevant information.

Arguments by the IP

- IP in his reply vide letter dated 13 July, 2020 submitted that the Corporate Debtor filed its financial statement for the financial year 2016-17 from which it was evident that the Corporate Debtor had considerable inventory, but the details of inventory were not available**.** He contacted the ex-directors of the Corporate Debtor to provide the inventory details. The ex-directors of the Corporate Debtor provided a list of properties situated at 25 locations which contained details of more than 2500 deeds. However, title deeds of most of these properties were not submitted till the end of the CIRP period.
- NCLT petition was filed against the ex-directors for non-cooperation. Pursuant to the order, 180 title deeds of properties located at seven locations in two parts were submitted to IP
- The valuer appointed for valuation purposes could not locate the assets due to non-demarcation and incomplete details and therefore demanded additional documents.
- Throughout the CIRP period, despite the best effort to take custody of the assets – other title deeds were not provided which amounted to more than 92 percent of the total title deeds with the ex-directors.
- The ex-directors failed to cooperate and despite repetitive initiatives, they delayed and refused submission of various relevant documents and information.

- Relying on advise that once the resolution for liquidation is passed by Committee of Creditors (CoC) members, further application w.r.t. non-cooperation can only be initiated once the liquidation order is passed by NCLT. Hence, no action was initiated under the relevant provisions of the Code even after NCLT's recommendation that appropriate course of action, should be initiated under the Code.
- That he has been suffering serious illness since June, 2018 after admission of CIRP of the said Corporate Debtor which caused delays in actions during the CIRP period.
- That the mistakes committed were bonafide with no malicious intent.

Held

- DC of the IBBI noted that an IP plays a crucial role in the CIRP and liquidation processes under the Code. He takes important business and financial decisions that may have a substantial bearing on the interests of all stakeholders. In such a scenario, it becomes imperative for an IP to perform his duties with utmost care and diligence.
- It is the duty of an IP to manage, preserve and protect the assets of the Corporate Debtor u/s 18, 20 and 25 of the Code.
- It is the duty of the IP to take reasonable care and diligence while performing his duties and to observe the provisions of the Code and the regulations.
- The UNCITRAL Legislative Guide on Insolvency Law emphasis the role of an 'insolvency representative' in the following words:

  "The insolvency representative plays a central role in the effective and efficient implementation of an insolvency law, with certain powers over debtors and their assets and a duty to protect those assets and their value, as well as the interests of creditors and employees, and to ensure that the law is applied effectively and impartially. Accordingly, it is essential that the insolvency representative be appropriately qualified and possess the knowledge, experience and personal qualities that will ensure not only the effective and efficient conduct of the proceedings and but also that there is confidence in the insolvency regime."

- Bankruptcy Legislative Reforms Commission (BLRC) report which led to the enactment of IBC has also emphasised on the role of an IP
- It was noted that the contention of the IP that despite having title deeds of 180 plots of land for seven locations, he could not take control and custody of the property for the reason of non-cooperation of the ex-directors in the identification of these plots is not tenable
- DC also pointed that NCLT in its order dated 29 October, 2018 found that IP did not make any efforts to investigate and identify the landed properties of the Corporate Debtor by appointing professionals from qualified surveyors or revenue authorities for collection of details regarding the landed properties, etc. In submission as well, IP had not mentioned any concrete efforts being taken nor any evidence was produced which may prove that efforts were taken

to take control and custody of the lands of the Corporate Debtor

- DC also pointed that IP should have approached the revenue authorities to inform them about the appointment of IRP and authority to take control of the assets of the Corporate Debtor. IP should have appointed surveyors for identification of the properties based on the 180 title deeds which were provided by the ex-directors. Moreover, despite the statutory duties under sections 18(1) and 25(1)(a), he failed to do so. This lapse on the part of IP has pushed the Corporate Debtor into liquidation as observed by the NCLT order (supra).
- IBBI stated that the IP`s conduct in making no material effort to identify and take control of the Corporate Debtors assets due to non- cooperation of ex-directors and failure to bring the said fact to NCLT`s notice "reflects his professional incompetence and negligence."
- IBBI barred the IP from accepting any assignments under IBC for 6 months, for his failure to take control of the corporate debtor`s assets despite statutory duties enshrined under IBC, thereby frustrating the whole of CIRP and pushing corporate debtor into liquidation and highlighted that without collection of information the IP cannot determine the financial position of the Corporate Debtor and thereby cannot take the custody of the assets which is the most important and primary duty as an IP.

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