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MMJC

Index

Report on Corporate Social Responsibility in e-form CSR-2

Ministry of corporate affairs (MCA) vide notification dated 11th February 2022, has amended the Companies (Accounts) Rules 2014. With this amendment new sub-rule (1B) has been inserted in rule 12 of in the said rule which became effective from 11th February, 2022.

Applicability:
The rule is applicable to all companies covered under section 135(1) of the Companies Act, 2013 (the Act).
Every which under the scope of section 135(1) of the Act is required to furnish a report on Corporate Social Responsibility (CSR) in e-Form CSR-2 to the registrar as an addendum to Form AOC-4 or AOC-4 XBRL or AOC-4 NBFC (Ind AS) as the case may be.

Filing:

- **For the Financial Year 2020-21** – e-Form CSR-2 shall be filed separately on or before **31st March, 2022**
- **For the Financial year 2021-22 onwards** – Form CSR-2 shall be filed as an **addendum** to Form AOC-4 or AOC-4 XBRL or AOC-4 NBFC (Ind AS), as the case may be.

Conclusion:
It is to be noted that most of the disclosures mandated in e-form CSR-2 are already being disclosed as a part of directors' report. It seems to be that the rolling out of e-Form CSR-2 is an effort towards collating the information which will provide comprehensive picture w.r.t. CSR funds spent and activities carried out. It will help MCA to undertake data mining and analysis of the same.

CRITICAL ASPECTS POST MERGER/AMALGAMATIONS UNDER THE COMPANIES ACT, 2013

Merger /Amalgamations transactions requires lot of pre planning of compliances and thoughtful actions on every aspect. There are some compliance areas under the Companies Act, 2013 (the Act) which requires detailed understanding of the provisions for planning the transaction of Merger /amalgamations.

There are various cases wherein it is established that scheme of merger is a code in itself.**In*Maneckchowk and Ahmedabad manufacturing Co. Ltd (1970) 40 Com Cas 819 (Guj) it was established that section 391 of Companies Act, 1956 is a code in itself.***However, there are various other provisions under the Act which are to be complied separately or shall be expressly covered in scheme wherever possible. we will see some of such areas or aspects and how one should deal with it.

A. Related Party Transactions of Transferor Company:

One of the critical aspects which should be taken care cautiously is Related Party transaction of Transferor and transferee Companies,

1. At the planning stage of Merger /Amalgamation transaction, one should check whether any entity or person with whom transferor / Transferee Company has transactions is becoming a related party of transferee Companies post-merger.
2. Transferee Company shall plan the Omnibus Approval limits of Audit Committee for related party transactions considering the absorption of transaction of Transferor Company for the year in which the transaction will get effective.
3. If the transactions are becoming material related party transactions, then Transferee Company shall plan the shareholder's approval before the effective date of the scheme.

MCA vide General Circular no. 30/2014 dated 17th July, 2014 has *clarified that transactions arising out of Compromises, Arrangements and Amalgamations dealt with under specific provisions of the Companies Act, 1956/Companies Act, 2013 will not attract the requirement of section 188 of the Companies Act, 2013."*

The aforementioned clarification states that any transaction arising out of *Compromises, Arrangements and Amalgamations* transaction (Capital reductions, allotments pursuant to merger or transfer of Assets pursuant to merger etc.) will not be considered as related party transaction and will not attract the requirements of Section 188 of the Act, but the transaction of transferor and transferee company which are continuing in nature be considered separately and would require compliance approvals separately.

B. Limits under Section 180/186 of the Act (Powers of Board):

Section 180 and Section 186 of the Act lays down the limits of borrowings and Loans, Investments, Guarantees & securities (LIGS) respectively for a company. Any borrowings and LIGS beyond the limits shall require the approval of the members of the Company in the manner laid therein.

Pursuant to merger /amalgamation all the borrowings and LIGS of transferor company will come into transferee company and the limitsapproved by members of transferee company or in existence thereof may exceed and therefore members approval for the limits of section 180 and 186 of the Act post-merger/Amalgamations shall be plan accordingly or the approval of limits under section 180 and 186 shall be taken as a part of scheme itself.

C. Section 185 of the Act:

Section 185 of the Act gives two kinds of prohibitions for giving loans, guarantees and securities,

- One is strict prohibition and
- Other is conditional prohibitions (which is allowed on passing special resolution)

Further there are also some conditional exemptions given for both kind of prohibitions.

There may arise a scenario where the transferor company has given loan, guarantee or security to any entity in which director of transferee company is interested as explained in the section and accordingly atransferee company shall take care of such points and plan the compliances accordingly.

D. Corporate Social Responsibility:

A scenario may be rear but is likely possible where the compliances of spending on corporate social responsibility is not applicable on individual basis to either of transferor company or transferee company but on merging of both the companies the net profit / Net worth /turnover figures are exceeding the thresholds and a compliance question may arise in case where the appointed data is kept in past, therefore appropriate plan of action for compliances on the same should be ensured.

E. Managerial Remuneration:

One crucial and limit-based compliance under the Act for Public Limited Companies is Managerial Remuneration and the same may be impacted if a loss-making company is merged with profit making company and therefore one should prior to the transaction or at early stage shall calculate the limits of remuneration and plan the resolution of shareholders required in any to ensure the compliance in this regard.

Conclusion:

Whenever a Merger /amalgamation transaction is planned one should look at the compliances in a wholistic or in a 360 Degree manner. Above discussion shows some of the scenarios which may be overlooked and which may lead to non-compliance. Hence it is crucial to plan a transaction with a forethought,which would give a clearer picture of all the areas of compliances having impact.

Sulochana Gupta and Minakshi Gupta V. M/s RBG Enterprises Private Limited, M/s. RBG Trading Corporation Private Limited, M/s. RBG Retail Private Limited and others NCLT Kochi Bench Order dated 31st December, 2021

Facts of the case:

- Respondent Companies against whom petitions were filed are family enterprises.
- During 2011, family dispute was started. Till then all were under the umbrella of HUF arrangement and all the family members were staying under one roof and acting in unison.
- During 2012 due to severe dispute among family members, 2nd and 3rd respondents (directors of respondent companies) were forced to leave the joint family house and started living separately and from that time efforts were going on for family partition of assets so that each of the co-parceners can proceed with their individual choices and business.
- Memorandum of Understanding (MOU) was signed on 15th September, 2016 after several rounds of discussions and deliberations. Essence of MOU was that business entities are to be partitioned and those that are presently controlled and managed by the family members will in so far as possible be retained by the same person.
- Petitioners are shareholders of the respondent companies. The Petition was filed against 3 different companies and their directors and the reliefs sought are against the oppression and mismanagement in the said respondent Companies which are more or less same. Reliefs sought are as follows:
  - To direct by an order that a meeting of shareholders to be convened and conducted under the supervision of this tribunal to undertake below businesses:

a. Board of Directors of respondent companies to be reconstituted
b. Obtain approval of shareholders for all Related Party Transactions (RPT) for the financial years 2015-16, 2016-17 and 2017-18
c. Appoint a new auditor to scrutinize all transactions and to conduct audit of the Accounts of the Company for the year 2015-16, 2016-17 and 2017-18 and to finalise / restate the accounts for said years within stipulated period after re-opening of the same.
d. To appoint new Internal Auditor
e. To select a Company Secretary to render advice on statutory compliances

- Direct to cancel all agreements, guarantees entered into with or on behalf of related parties which might not approved by the shareholders
- Direct 2nd respondent (being Managing Director) and 3rd Respondent (one of the Director)

(a) to Refund to respondent companies the amounts received as a part of director remuneration and directors' relatives' remuneration or w.r.t. other RPTs for the financial years 2015-16, 2016-17 and 2017-18 which might not get approved by the shareholders

(b) to get Remittance of amount of Rs. 1,92,00,000 to the respondent companies - Rental Income due from Sri Rubber Industries (Partnership Firm of 2nd and 3rd Respondent) for the period from 2010 to 2018, for occupying the warehouse.

(c) To get Remittance of amount of Rs. 36,00,000 – Rental Income to RBG Trading Corporation Private Limited (2nd Respondent Company)

- Reopening of financial statements and Annual Accounts for FY 2015-16, 2016-17, 2017-18 u/s 130 of Companies Act, 2013
- Initiate action u/s 99 for not complying with Sec. 96 of Companies Act, 2013, i.e., not holding annual general meetings and representing that those were held, to the Registrar of Companies as a part of filings of financials and annual returns
- Initiate action u/s 448 against 2nd and 3rd respondents for false statement and reports for FY 2015-16, 2016-17, 2017-18
- Initiate Action against the 2nd and 3rd respondents for failure to disclose interest u/s 184 of the Companies Act, 2013
- Initiate action u/s 185 – for failure to report to shareholders for RPT transactions during FY 2015-16, 2016-17, 2017-18

Arguments by Petitioner
The councils on behalf of petitioner argued that:

- 2nd Respondent is Managing Director (MD) who is in collusion with 3rd respondent (director)has been managing the respondent companies in a manner prejudicial to the interests of the public; and importantly to the interests of the Petitioners and other shareholders.
- As per the Companies Act, 2013 ('the Act') and the Articles of Association, respondent companies are to be managed by respective board of Directors but in reality, it is being run by 2nd respondent i.e. MD of respondent companies along with 3rd respondent, another director of respondent companies.
- Further it was argued that 2nd and 3rd respondent have flouted with AOA and Sec. 203 of Companies Act, 2013 and 2nd respondent appointed himself as MD of all 3 respondent Companies and also violated Sec. 173(3) by not sending notice and sending reminder 2 days before the meeting instead of notice.
- They had filed false documents with ROC to the effect that all AGMs have been conducted for the years 2016, 2017 and 2018, whereas it is argued that respondent has failed to hold AGM for many years. Further Documents which have been created are forged.
- AGM was held in 2019, wherein financial statements were approved by poll, but the outcome of the poll were not declared at all.
- Financial statements filed before ROC discloses Related Party Transactions (RPTs) which were entered in contravention of Sec. 188.
- 2nd and 3rd respondent siphoned huge amounts from the respondent companies in the guise of remuneration to themselves and to their spouses without the approval of the majority of the shareholders.
- Further following entities had occupied space in the warehouse of 1st Respondent Company without payment of the rent to the respondent company –
  - M/s Sri Rubber Industries which is a partnership Firm of 2nd and 3rd respondents and the rental income due from it is not disclosed in the financials. The Estimated amount of rent payable calculated @ approx. 2 lakh per month since 2010 which amounts to Rs. 1,92,00,000/-

- RBG Trading Corporation Private Ltd. had occupied since 2018 and the rental income due from it is not disclosed in the financials. Further estimated rental income due is Rs. 36,00,000/-
- All RPTs were done without obtaining approval of the majority shareholders of the respondent companies.
- It was stated that as the accounts do not represent accurate picture therefore accounts of respondent company deserves to be re-opened u/s 130

Arguments by Respondents:

- AGM was held for all the years (Since 2015-16 to 2017-18) and the said meetings were attended by the petitioners along with all family members and the relevant financial statements are also filed with ROC.
- All the allegations are arising out of family dispute only
  All the transactions are in Compliance of Sec. 188. Further Disclosed RPTs entered as follows:

Transaction	**Explanation provided by the Respondent**
Interest recd. From RPs	Company benefitted by pooling of resources as interest is charged at rate of 9-12% which is as per market standards
Loans given/refunded to RPs	Loans are Outside the scope of Sec. 188. Further it carries interest between 9-12% Pa. – Therefore, comes under commercial transactions – The said transactions are at arm's length pricing (ALP) and fully exempted under 3rd proviso of Sec. 188(1) Further Statutory Auditors have not made any adverse comment and are fully disclosed in financial statements
Remuneration drawn by MD	No violation of Sec. 188 as there is different section which governs remuneration and therefore co. is fully Compliant It is in compliance with the provisions of Companies Act and authorised by the Board

Commission received	For using storage space and open vacant spaces for export processing at the warehouse. As open spaces cannot be let out to outsiders – therefore it is benefitted to company
Remuneration paid to wives of MD and 3rd respondent	Full time employees assisting companies and they are qualified and considering workload paid remuneration In compliance of provision of Companies Act and authorised by the Board
Rental Income – Partnership	Name Board of Sri Rubber Industries was placed at the warehouse of respondent 1 company since 12 years but no activity is done at the warehouse and Name board was only kept for sales tax purpose – there was a name sake agreement which was signed incidentally by 2nd respondent The said Arrangement was made many years ago and well known to all stakeholders in RBG family group
Rental Income – RBG Trading	Rental income due disclosed in Balance sheet. Further respondents denied to pay rental income of 36 lakh as payment is made by way of commission for use of premises Arrangement was made many years ago and well known to all stakeholders in RBG family group

- It was stated that MBP-1 disclosing interest was available for all directors except one director who is husband of 2nd petitioner
- All family business concerns are known to all family members and there has not been a single entity other than family promoted concerns and all RPTs are disclosed in balance sheet of relevant years
- For re-opening books of accounts u/s 130 petitioners are required to place a proof of fraudulent matters before this tribunal rather than bringing the disclosed particulars available in the financials in public domain
- Appointment of MD is in full compliance of the provision of articles and in compliance of the provisions of the Act. Further 203 is not applicable to the respondent companies.
- All RPTs are commercial transactions which benefitted company and carried in the interest of the Company and all allegations are arose due to family dispute

Court held that:
Question of law raised by Court are as follows:
Issue No. 1- Whether the Company petition is maintainable?

- Respondent averred that Companies are eligible for certain limited exemptionsunder sections 185 and 188 of the Act based on erroneous interpretation of exemptions granted to Private Companies under MCA notification dated 5th June, 2015.
- The exemption will be applicable to a private company **only if the interest of their shareholders are protected.**
- Further the Tribunal went through various RPTs which would reveal that 2nd and 3rd respondents siphoned funds to the prejudice of the shareholders.
- Hence no exemption can be claimed based on said notification.

Issue No. 2- Whether 2nd respondent violated the provisions of the articles of association ('AOA') of the 1st respondent company?

- AOA is important document and all the powers of directors and other officials and also rights and obligations are prescribed in AOA. So, AOA holds key importance in any company or organisation as whole internal management is done in accordance with it.
- It is crystal clear that AOA of respondent companies that the business of the Company shall be managed by the Board of directors; and the directors of the Company act as trustee on behalf of Company in fiduciary capacity.
- It is found that AGM of companies have not been held. AGM gives opportunity to shareholders to know the condition of the Company and also make suggestion for its improvement and progress.
- Further it was observed that Respondent failed to provide any evidence to show that the notice of AGM was issued to all the shareholders including the petitioners in the manner prescribed by the statute
- Therefore, the Tribunal concluded that respondents have violated provisions of AOA.

Issue No. 3- Whether there is related party transaction in the Company?

- The Tribunal noted the definition of Related Party and Sec. 188, and also RPTs disclosed in financial statements filed with ROC.
- The required approvals of Board of Directors andthe shareholders, wherever applicablewere not obtained for entering into RPTs and same was also not disclosed in Board's report and Register of Contracts maintained under the Act.
- Hence, it was held that RPTs entered were contrary to the provisions of law and in breach of AOA. Therefore RPTs were declared invalid and proceedings which have been done in violation of AOA were hereby also declared as invalid.

Order in the matter of Telangana State Trade Promotion Corporation (Appellant) Vs. A.P. Gems & Jewellery Park Private Limited & Anr (Respondent) as passed by the National Company Law Tribunal (NCLAT) Chennai on21st September, 2021

Facts of the case:

- The Phoenix Tech Power Limited - Financial Creditor (FC/Second Respondent) made an application u/s 7 of the Insolvency and Bankruptcy Code 2016 (IBC/Code) to initiate a Corporate Insolvency Resolution Process (CIRP) against A.P. Gems & Jewellery Park Private Limited - Corporate Debtor (CD)
- The application was admitted by the National Company Law Tribunal Hyderabad Bench (NCLT) on 4June, 2019.

- Telangana State Trade Promotion Corporation (Appellant) is the Promoter and 5.1% shareholder of the CDand having two nominee non-executive directors on the board of CD
- The appellant had allotted land to CD for ₹12,77,91,125/- and as a part of settlement of land cost appellant was allotted 2,75,000 equity shares ₹ 10/- each and 9,15,000 Preference shares of ₹ 10 each. The balance consideration of ₹ 11,58,91,125/- was treated as unsecured loan. It was on account of this loan that the Appellant was included as memberof Committee of Creditor (CoC).
- Interlocutory application was filed at the NCLT by the second respondent - FC. NCLT noticed that the some of decisions in the Articles of Association (AoA)of the CD are required to be taken by affirmative votes of three or more directors including one director nominated by appellant.
- NCLT also observed that nominee directors of Appellant have significant influence in the functioning of the CD. It was accordingly concluded that the appellant is a 'related party'and directed Resolution Professional (RP) to reconstitute the CoC by treating appellant as a related party.

- The Appellant aggrieved by the order of NCLT filed an appeal against the order at NCLAT.

Arguments by the Appellant:

- NCLT has committed an error in concluding that the Appellantrepresented through one nominee Director (i.e. Mr. Saida V) has significant influence.
- NCLT should have appreciated the appellant as a 'Financial Creditor' u/s 5(7) of the Code. However, wrongly determined Appellant as a 'related party' u/s 24(5)(a) of the code.
- Pointed out that the appellant hold 5.1% 'equity shares' and 5.9% 'preference shares thereby holds 11% voting right(s) on account of 'ownership' and such a small percentage cannot be considered and declared as having a significant influence in the affairs of the CDand henceSection 24(5)(j) of the code is not applicable.
- Appellant adverts to Article 62 of the AoA which provides that there must be at least one director of the Appellant in the minimum 'quorum' of three and that

such 'right of representation' cannot be construed to mean as a right of majority.

- The clause of AoA provides for an affirmative voting right to protect its investment and envisages no control to the Appellant over the CD and these rights are negative rights, given to the Appellant. Also added that the protective provision under AoA was not in the nature of day-to-day operational control over the CD business. Such provision merely enablesthe Appellant to oppose a proposal. In fact, it is conventional for the financialinvestors to protect their investment from the whims and fancies of the'promoters' that manage the CD.
- Also added that NCLT hadincorrectly observed that there are two nominee directors of the Appellant and they hadsignificant influence in the decisions making process of the CD.CD was neither inclined nor accustomed to Act on the advice of directors or instructions of the Appellant.One Nominee director on the Board of the CD out of the minimum quorum of three, couldconcluded that the 'Appellant' had 'Veto Power' in the Board.
- Therewas neither participation in policy making of the CD by the Appellant nor there was interchange of managerial personnel between the Appellant and the CD.
- There wasno exchange of technical of information to or from, to the CD to the Appellant.
- The term "control" employed under Section 5(24) of the code was to be interpreted in accordance with the definition provided under the Companies Act, 2013 (the Act) but not debtors however NCLT had traversed beyond the provisions of the Act, to hold that the Appellant wasa 'related party'.

Arguments by the CD/Respondent

- RPhad initially not included the Appellant as part of their CoC as it was being examined by the RP whether the 'Appellant would fall within the meaning of 'related party' as defined u/s 5(24) of the Code but based on the documents provided by the Appellant and on being satisfied that the Appellant was not falling within the meaning of 'related party',the RP in the 7th CoC Meeting included the Appellant as a Member of the CoC.
- The representative of the FC was also present but he had not expressed any objection or concern over the inclusion of the Appellant as a Member of the CoC.
- Not raising any objection before and raising it at this stage before NCLAT at inordinate stage of CIRP.
- The definition of a 'related party' as per the Act and as per Accounting Standards cannot be relied upon to establish that a party is a 'related party' under the provisions of the Code and that the provisions of theCode over ride other laws laid down under Section 238 of the Code.
- FCis in no manner affected by the inclusion of the Appellant as a member of the CoC, as the whole process of CIRP is to be carried out as per the ingredients of the Code. Besides this, all the meetings of the CoC were validly held.

Arguments by Second Respondent Submission

- Appellant was not a mere shareholder but a controlling partner who had a definitive say and control in the affairs of the CD.
- The presence of twodirectors out of five directors on the Board of the CD itself makes the Appellant a 'related party' as contemplated in the Code.
- Many of the policy decision cannot be taken without the affirmative vote of at least one director nominated by/representing the Appellant as per the Article 62

of the AoA.

- Article 70 and 71 of the AoA of the CD conferred special power upon the CD as to auditing the CD and also the appointment of statutory auditors of the CD. Further, the appellant had control the composition of Board of Directors of the CD as per Clause62(a) of AoA. Thus, composition of the Board of Directors wasunder the control of Company.
- Appellantwas a body corporate whose Managing Director was also a Director of the CD and the other Directors nominated by the Appellant also advices the Appellant in issues concerning with the CD. The double role of the two nominee Directors clearly establishes that the CD acts on the advice, direction and instructions of the Appellant in its ordinary course of business in issues relating to the CD. Assuch, it is a 'related party' as per 5(24)(f) of the Code.
- CD had been treating the Appellant as a 'related party' and had reported the transactions between them as 'related party' transactions in a statutory document such as annual reports and audited financial documents and the same is reported as per the definition of 'related party' under the Act mandatory accounting standards. Further, the definitionof the 'related party' under IBC is adopted from the definition of the 'related party' under the 'the Companies Act' after making modification to suit the context.

Vital Element raised by NCLAT:

- An essential element in regard to the exercise of control is the power to appoint majority Directors and power to influence to the policy decision of Company. In fact, the word 'control' in Section 2(27) of the Act includes exercising the right to appoint majority of Directors on the Board of Companies or controlling the management or policy decisions of the Company by a person or persons acting individually or in concert, it is to be remembered that the power may be exercised by a person or persons either directly or indirectly. It may flow by virtue of their shareholding or their management rights or shareholders' agreements, voting agreements or in any other fashion.
- The power to control the composition of Board of subsidiary company could arise from the voting rights enjoyed by the holding Company by virtue of shares in the subsidiary held by it or its nominees or from the provisions contained in the Memorandum or Articles or from the terms of contract with the subsidiary which confers rights on the holding company to appoint the Directors on the Board of subsidiary Company vide decision Oriental Industrial Investment Corporation Ltd. vs. Union ofIndia
- Anyone who by exercise of voting power can control the decisions of a General Meeting can be said to 'control' the Company. A person can be said to be in control of Company when there was no matte or perhaps no substantial matter on which he could be outvoted at a General Meeting. Moreover, when Directors of a Company hold majority of shares which under AoA carry voting right, then, they can be said to have controlling interest.
- ***The real test is whether a person controls either the steering or the accelerators, gears and brakes. If the answer is in the affirmative, then he would be in the 'Control of Company' in the considered opinion of this Tribunal***

HELD

- The expression 'control' in Section 29A(c)of the Code symbolizes only the positive control i.e. that the mere powerto block special resolutions of a Company cannot amount to control. In reality,the word 'control' juxtaposed with the term 'management' means 'De factocontrol of actual management or policy decisions that may be or are in realitytaken.
- The part played by the two nominee directorsclearly point out that the CD acts on the advice,direction and instructions of the Appellant in its normal business affairsrelating to the first Respondent. As such, NCLAT is of the earnestopinion that the Appellant 'squarely comes within the ambit of related party as per 5(24)(f) of the Code.
- The other important fact that cannot be brushed aside is that that the CD had reported the transactions between the Appellant andit, in their 'Annual Reports' and 'Audited Financial Statements'. Besidesthis, as perceived from the AoA and the requisite majorityneeded for taking important business decisions, the conduct of the business of the CD, the establishment of CD all considered in an integral and cumulative manner will exhibit thenoteworthy influence of the Appellant in issues concerning the CD. In this manner also, the CD is treating theAppellant as 'Related Party.
- The Appellant has a control in regard to the arrangement of Board of Directors of the CD and the Appellant comes within the purview of 'related party' u/s 5(24)(L) of the code as opined by NCLT.
- The AoA points out that action relating to significant matters ought to be taken only by affirmative vote of three or more Directors and in the qualified majority, minimum one Director is to be nominated for inclusion by the Appellant.
- The nominee Directors have a vital influence in regard to the working of the CD, Appellant is a 'related party' and the view arrived at by the RPto include the Appellant as member of the CoC is clearly unsustainable in the eye of law.
- Thereby the appeal was dismissed and the order of NCLT was upheld.

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