CS Makarand Joshi

CORPORATE LAWS

Case Law Update

SEBI

Name of the Case: Final Order of the Whole Time Member in the matter of Coral Hub Ltd.

Facts of the case

1. **Inflated and Fabricated figures of sales**
Securities and Exchange Board of India ('SEBI') was in receipt of complaint inter-alia alleging that revenues and profit of Coral Hub Ltd ['CHL'/'the Company'/Noticee no. 1'] were fabricated and artificial. SEBI conducted an investigation in this regard from April 1, 2008, to June 30, 2010. On investigation, SEBI alleged that CHL had published false, inflated, and misleading financial results during Financial Year 2008-09 and 2009-10. SEBI further alleged that during these years, CHL had shown false and inflated sales figures, and due to this, figures of profit carried over in the balance sheet were also inflated. SEBI stated that CHL was making sales inter-alia to two entities viz. Food and Agriculture Organisation, UN ('FAO') and NDS USA LLC ['NDS']. SEBI alleged that sales to FAO were inflated to the extent of ₹ 38.22 crore, and NDS was inflated to the extent of ₹ 32.99 crore. SEBI further alleged that these inflated figures cumulatively constituted 51.90% of total sales for FY 2008-09 and FY 2009-10.

2. **Non-disclosure of Related Party Transactions**
On investigation, SEBI alleged that there was a violation with respect to the disclosure of related party transactions. SEBI observed that Raydox Technologies FZ LLC ['Raydox'], Avington Solutions Ltd (UK) ['Avington'], and Rochelle Associates Ltd (UK) ['Rochelle'] had Mr. Anthony Lopes as Director. Mr. Anthony Lopes was also Manager Administration of Tutis Technologies Ltd ['TTL'], promoter entity of CHL. Mr. Anthony Lopes submitted to SEBI that Raydox, Avington, and Rochelle were companies set up and controlled by directors of CHL, viz., G.S.Vishwanatham, Whole Time Director ['GSV/Noticee no.4'], Mr. G.S. Chandrasekhar, Non-Executive Director ['GSC/Noticee no.2'] and Dilip C Parekh, Whole Time Director ['DCP/Noticee no. 3']. Thus SEBI alleged that being related parties of CHL, sales made to Raydox, Avington and Rochelle were not

disclosed in Annual Report for 2009-10 under Related Party Transactions.

3. **The allegation in respect to Misstatement regarding Board Meetings**
SEBI on investigation observed that in Annual Report of 2009-10, it was mentioned that fifteen board meetings were held. In this Annual Report, it was mentioned that Mr. D.M. Shirodkar, Independent Director ['Noticee no. 5'], Mr. Harish Sahu, Independent Director ['Noticee no.6'] and Mr. Ghanshyam Joshi, Independent Director ['Noticee no. 7'] had attended five, twelve, and fifteen board meetings, respectively. But SEBI had received written replies from Noticee no. 5, Noticee no. 6, and Noticee no.7 stating that they never attended any Board Meeting. Further Noticee no. 3 had also given a written statement that since 2008 no formal Board Meeting was held. Taking into consideration all the above allegations SEBI issued a Show Cause Notice ['SCN'] to CHL and Noticees ['Noticee no.1 to Noticee no.7'] dt: October 30, 2015, as to why appropriate directions under Section 11(4) and 11B of SEBI Act, 1992 should not be issued against Noticees.

Charges levied

Noticees have violated the provisions of Section 12A (a), (b) and (c) of SEBI Act, 1992, Regulation 3(b), (c) and (d) read with Regulation 4(1) and 4(2)(e), (f), (k) and (r) of Prohibition of Fraudulent and Unfair Trade Practices Regulations, 2003 ['PFUTP'], Clause 32, Clause 49 of the Listing Agreement read with Section 21 of Securities Contract Regulations Act, 1956 ['SCRA 1956'].

Arguments made by Noticees

1. ***Inflated and Fabricated figures of sales***
Noticee no. 2 stated that Noticee no.3 is alone responsible for inflated invoices as he was in charge of sales, accounts, finance, production, administration from the year 2000 till July 2012. He was also singular signing authority for all bank transactions. So Noticee no.2 stated that Noticee no.3 could have created fake P.O. for client, fudged production records, and accordingly instructed accounts to prepare invoices and would have convinced auditors about the sanctity of transactions. Noticee no. 2 further stated that the contract with FAO ran for almost 10 years. Noticee no. 3 used to brief the Board of Directors that CHL gets work from FAO offices globally. Also, he used to mention that NDS used to give large projects to CHL. Noticee no.3 denied all allegations made by Noticee no.2 and stated that Noticee no.2 only was responsible for inflated invoices. Noticee no.3 stated that Noticee no.2 was dealing with issues domestically within India or overseas. Noticee no.3 further stated that it was Noticee no.2 who used to decide what should be told to auditors and also managed to get signatures from the Auditors and Company Secretaries. Noticee no.4 stated that his association with the Company was purely professional, and responsibility was restricted to technical aspects only. Noticee no.4 said that he is aware that FAO and NDS were clients of the Company as sales were done to them, but he denied being aware of inflated billings as they were handled by Finance and Accounts. Noticee no. 5, Noticee no.6, and Noticee no.7 did not reply on this aspect.

2. ***Non-disclosure of Related Party Transactions with Raydox, Rochelle, and Avington***

Noticee no. 2 and 4 submitted that they were not related to Avington and Rochelle. These entities cannot be considered as related parties. Noticee no.2 denied the statement made by Mr. Anthony Lopes that Noticee no. 2 was giving instructions with respect to the functioning of Avington and Rochelle. Also, he denied the statement that Noticee no.2 was whole & sole for Rochelle. Noticee no. 2 further sought to cross-examine Mr. Anthony Lopes on what basis he was making these statements. Noticee no. 2 further stated that he was not aware of any sales made to Avington as he was not involved in sales and marketing. Noticee no. 2 and 4 submitted facts with respect to Raydox. Noticee no. 2 accepted that he was director of Raydox between 2003 to 2007. He further submitted that he resigned from directorship in 2007. As against this, Noticee no. 3 submitted that statements made by Mr. Anthony Lopes and Mr. Sutesh Nair were true. Further, Noticee no. 4 stated that Raydox was formed in 2003 by Noticee no. 2 and 4 in UAE. Noticee no. 4 further stated that he and Noticee no. 3 were directors in Raydox till the end of 2005. Then both of them resigned from Raydox. He further submitted that CHL had no investment in Raydox, and post 2005, Raydox was managed by Mr. Anthony Lopes.

3. ***The allegation in respect to Misstatement regarding Board Meetings***

Noticee no. 2 submitted that he had attended many Board Meetings. Further, he submitted that Noticee no. 5, 6 & 7 had attended many board meetings in Mumbai and in Chennai. Noticee no. 2 also brought to the notice of Whole-time Member, SEBI ['WTM'] that there was an attendance register for board meetings, and every director used to sign it. Noticee no. 3 stated that no formal board meetings had been conducted since April 2008. Noticee no.2 further requested SEBI not to conclude only on the basis of statements made by Noticee no. 5, 6 & 7. Noticee no. 5, 6 & 7 in their preliminary submission had mentioned that no board meetings were held at CHL. But Noticee no. 5 and 7, while making submissions before WTM, stated that they had attended a few board meetings. Noticee no.6 continued to state that he did not receive any communication regarding any board meeting from CHL.

Conclusions made by Whole Time Member, SEBI

1. ***Inflated and Fabricated figures of sales***

WTM noted that Noticees have not denied of having business with FAO and NDS rather, they have stated that FAO & NDS were clients/customers of CHL since the year 2001 & 2004, respectively. WTM further held that none of the Noticees have submitted any proof regarding the receipt of payment of (a) approx. ₹ 38.22 crore for sales made to FAO by CHL for FY 2008-09 and FY 2009-10 and (b) approx. ₹ 32.99 crore for sales made to NDS by CHL for FY 2008-09 and FY 2009-10. FAO vide its email dt: October 23, 2013, stated that the total amount paid to CHL from July 2001 till December 2009 was US$ 2,98,301.50 (taking conversion ratio @ ₹ 50/dollar at the relevant time), the

total amount comes to ₹ 1,49,15,075/- and NDS vide its email dt: October 7, 2013, stated that NDS was a client of CHL prior to and up to May 2007. The last payment made to CHL was in June 2007. Further, WTM held that Noticees have neither denied nor submitted any documentary evidence to negate the email confirmation of clients FAO and NDS. So WTM concluded that in the absence of any proof of receipt of payment from FAO and NDS, coupled with evidence of email confirmation regarding payment of ₹ 1.49 crore by FAO to CHL during July 2001 till December 2009 and looking at the fact no payments were made by NDS to CHL post-June 2007, amount of sales made to FAO and NDS by CHL in FY 2008-09 and FY 2009-10 were inflated to the extent of Rs 71.21 crore (approx.), **i.e., 51.9%**

2. ***Non-disclosure of Related Party Transactions with Raydox, Rochelle, and Avington***

WTM first decided to conclude on the existence of Raydox, Rochelle, and Avington as there were a lot of arguments made on their existence.

(a) Whether Raydox was related Party, if yes, is there any violation?

WTM noted that Mr. Anthony Lopes had confirmed that he was director of Raydox during the FY 2008-09 and 2009-10, and Raydox was set up by Noticee no.2 and 4. Further, WTM noted that Noticee no.2 and Noticee no. 4, in their submissions, have stated that they have formed Raydox, and Noticee no. 2 was investor/shareholder of Raydox. Further, Noticee no. 2 & 4 had not submitted any documentary evidence that Noticee no. 2 had ceased to be a shareholder also of Raydox. Thus WTM stated that in the absence of lack of submission of documentary evidence by Noticee no. 2 that, he had ceased to be a shareholder of Raydox and the fact that Noticee no. 2 and 3 were directors of CHL and TTL during 2009-10 (source: MCA database and Annual Report of CHL and TTL) exercised control through Mr. Anthony Lopes over Raydox during FY 2008-09 and 2009-10, it could be concluded that Raydox was a related party during FY 2008-09 and 2009-10. Further, WTM noted that Noticee no. 2 stated that he resigned as a director of Raydox in 2007, while Noticee no. 4 stated that Noticee no. 2 resigned at the end of 2005 along with Noticee no.4. Thus WTM denied accepting resignation dates given by Noticee no.2 and Noticee no.4 in the absence of documentary evidence. WTM further stated that sales made to Raydox amounting to Rs 22.95 crore (37.57%) in FY 2008-09 and ₹ 21.99 crore (28.93%) in FY 2009-10 was not disclosed under the head-related party transaction. Thus, the allegation that CHL failed to disclose the sales made to Raydox under the head-related party transactions in AR for FY 2009-10 stands established.

(b) Whether Avington and Rochelle were related Party, if yes, is there any violation?

WTM stated that Financial Conduct Authority ('FCA, UK') vide its email dt: September 23, 2013, informed SEBI that they were not finding any existence of Avington Solutions Ltd and Rochelle Associates Ltd. WTM further noted that as no documents/information regarding the existence and control of Avington and Rochelle has been available, reliance is placed on the statement of Mr. Anthony Lopes (who was Manager Administration of Promoter entity of CHL, as mentioned in the facts of the case) and Mr. Sutesh Nair (who was VP – Finance & Accounts of CHL). Further, WTM noted that Noticee no.2 has submitted that Avington and Rochelle are not UK-based entities. Further, WTM noted that Noticee no. 2 has also submitted that he had no connection with/ control directly or indirectly over Avington and Rochelle. Avington was neither promoted nor set up by Noticee no. 2 or Noticee no. 3 or Noticee no. 4. None of the directors of CHL were involved in Avington affairs directly or indirectly. WTM took note of the fact that Noticee no. 2 sought to cross-examine Mr. Anthony Lopes with regard to his statement of involvement of Directors of CHL in the formation of Avington and allegation that Noticee no. 2 was whole & sole of Rochelle. But WTM also noted that Noticee no. 2 was not given an opportunity to cross-examine Mr. Anthony. So as per the principles of natural justice, WTM concluded that the statement of Mr. Anthony Lopes to the extent of Noticee no. 2's involvement in Avington and Rochelle could not be relied upon. WTM further stated that apart from the statement of Mr. Anthony Lopes, there is no other documentary evidence regarding the existence of Avington and Rochelle and they being controlled by CHL or any of its directors. Hence in view of fair proceedings and in the absence of documentary evidence, it is difficult to conclude that Avington and Rochelle were related parties of CHL during FY 2008-09 and FY 2009-10. Thus the allegation that CHL failed to disclose the sales made to Avington and Rochelle under the head-related party transactions in AR for FY 2009-10 does not stand established.

(3) The allegation in respect to Misstatement regarding Board Meeting:

WTM took note of submissions made by Noticee no. 2 to Noticee no.7. WTM noted that Noticee no. 3 and 6 had not submitted any documentary evidence to prove that no board meetings have been conducted since April 2008. WTM stated that as against this, Noticee no. 2 has submitted a copy of signed and unsigned minutes of some board meetings held since 2008 and copies of board resolutions. WTM also highlighted that CHL had made various announcements on conducting board meetings to Bombay Stock Exchange ['BSE'] and National Stock Exchange

['NSE'] during FY 2008-09 and FY 2009-10. Dates of these board meetings, for whom the disclosure was given on BSE and NSE matched with dates of signed and unsigned minutes submitted by Noticee no. 2. WTM, on comparison of minutes of board meeting minutes and disclosure from stock exchange website concluded that around 32 board meetings were conducted during April 1, 2008, till June 30, 2010. WTM further noted that dates of board meetings of CHL mentioned in the annual report of 2010 matched with dates of board meeting minutes submitted by Noticee no. 2 except for board meeting dt: June 11, 2010, whose minutes were not submitted but the outcome was available on BSE website. So WTM concluded that the allegation of violation of provisions of Clause 49(C)(i) of the listing agreement read with Section 21 of SCRA 1956 against CHL does not stand established.

(4) Observations by WTM

Cash flow from operations was declining consistently even when sales were increasing, and there was an increase in debtors by almost double within a period of six months. These instances should have acted as a red flag for members of the Audit Committee (viz. Noticee no. 5, 6 & 7). This should have prompted them to raise questions to auditors. This shows that Noticee no. 5, 6 & 7 were grossly negligent. WTM further stated that going by the submission of Noticee no. 5, 6 & 7, they did not receive board meeting/audit committee meeting notice, then the question arises why didn't Noticee no. 5, 6 & 7 ask CHL as to why meetings are not being conducted? Noticee no. 2 & 4 have blamed that CHL was being run as a sole proprietary concern by Noticee no.3. They had full faith in Noticee no. 3. WTM stated that this submission of Noticee no. 2 & 4 cannot be accepted. WTM stated that it was the role of Noticee no. 2 to Noticee no.7 as Board members, Committee members, and signatories to various documents to ensure that affairs of CHL are carried out properly. Noticee no. 2 to 7 cannot escape from the obligation of CHL with regard to its fiduciary duties towards CHL and its shareholders. Noticee no. 2 to 7 have failed in their duty to exercise due care and diligence and allowed the Company to fabricate figures and make false disclosures.

Penalty No monetary penalty was levied

Noticee no.	Name of the entity	Debarment period
1	Coral Hub ltd	Three years
2	Mr. G.S. Chandrasekhar	Three years
3	Mr. Dilip C. Parekh	Three years
4	Mr. G.S.Vishwanatham	Three years
5	Mr. D M Shirodkar	Two years
6	Mr. Harish Sahu	Two years
7	Mr. Ghanshyam Joshi	Two years

IBC

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 on September 21, 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 June 4, 2019.
- Telangana State Trade Promotion Corporation (Appellant) is the Promoter and 5.1% shareholder of the CD and 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 the 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 an unsecured loan. It was on account of this loan that the Appellant was included as a member of the Committee of Creditors (CoC).
- An interlocutory application was filed at the NCLT by the second respondent - FC. NCLT noticed that some 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 the appellant.
- NCLT also observed that nominee directors of Appellant have a significant influence on 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 the 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 Appellant represented 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 holding 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 CD and hence Section 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 the 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 enables the Appellant to oppose a proposal. In fact, it is conventional for financial investors to protect their investment from the whims and fancies of the 'promoters' that manage the CD.
- Also added that NCLT had incorrectly observed that there are two nominee directors of the Appellant, and they had significant influence in the decisions making process of the CD. CD was neither inclined nor accustomed to acting 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, could conclude that the 'Appellant' had 'Veto Power' in the Board.
- There was neither participation in policy-making of the CD by the Appellant nor there was an interchange of managerial personnel between the Appellant and the CD.
- There was no 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 was a 'related party.'

Arguments by the CD/Respondent

- RP had 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 the 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 the Code override other laws laid down under Section 238 of the Code.
- FC is 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 two directors out of five directors on the Board of the CD itself makes the Appellant a 'related party' as contemplated in the Code.
- Many policy decisions cannot be taken without the affirmative vote of at least one director nominated by/representing the Appellant as per 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 the appointment of statutory auditors of the CD. Further, the appellant had controlled the composition of the Board of Directors of the CD as per Clause 62(a) of AoA. Thus, the composition of the Board of Directors was under the control of the Company.
- Appellant was a body corporate whose Managing Director was also a Director of the CD, and the other Directors nominated by the Appellant also advised the Appellant in issues concerning with the CD. The double role of the two nominee Directors 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. As such, 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 definition of the 'related party' under IBC is adopted from the definition of the 'related party' under the 'the Companies Act' after making modifications 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 the power to influence to the policy decision of the Company. In fact, the word 'control' in Section 2(27) of the Act includes exercising the right to appoint a 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 the 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 the 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 of India

- Anyone who, by the 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 the 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 the majority of shares which under AoA carry voting right, then, they can be said to have a 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 power to block special resolutions of a Company cannot amount to control. In reality, the word 'control' juxtaposed with the term 'management' means 'De facto control of actual management' or policy decisions that may be or are in reality taken.
- The part played by the two nominee directors clearly points out that the CD acts on the advice, direction, and instructions of the Appellant in its normal business affairs relating to the First Respondent. As such, NCLAT is of the earnest opinion that the Appellant' squarely' comes within the ambit of the related party as per 5(24)(f) of the Code.
- The other important fact that cannot be brushed aside is that the CD had reported the transactions between the Appellant and it, in their 'Annual Reports' and 'Audited Financial Statements.' Besides this, as perceived from the AoA and the requisite majority needed 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 the noteworthy influence of the Appellant in issues concerning the CD. In this manner also, the CD is treating the Appellant as 'Related Party.'
- The Appellant has control in regard to the arrangement of the 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 the affirmative vote of three or more Directors, and in the qualified majority, a minimum of 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 RP to include the Appellant as a member of the CoC is clearly unsustainable in the eye of law.
- Thereby the appeal was dismissed, and the order of NCLT was upheld.

Co's Act

Sulochana Gupta and Minakshi Gupta vs. 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 December 31, 2021

Facts of the case

- Respondent Companies against whom petitions were filed are family enterprises.
- During 2011, a family dispute was started. Till then, all were under the umbrella of the 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 September 15, 2016, after several rounds of discussions and deliberations. The 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 the 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 conduct an audit of the Company's Accounts for the year 2015-16, 2016-17, and 2017-18 and to finalize/restate the accounts for said years within a 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 be 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 a Remittance of the amount of ₹ 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 the amount of ₹ 36,00,000 – Rental Income to RBG Trading Corporation Private Limited (2nd Respondent Company)

— Re-opening 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 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 the petitioner, argued that:

- the 2nd Respondent is, Managing Director (MD), who is in collusion with the 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 respondents 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 was 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 respondents 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 ₹ 1,92,00,000/-
  - RBG Trading Corporation Private Ltd. has occupied since 2018, and the rental income due from it is not disclosed in the financials. Further estimated rental incomed due is ₹ 36,00,000/-
- All RPTs were done without obtaining the approval of the majority shareholders of the respondent companies.
- It was stated that as the accounts do not represent an accurate picture, therefore, accounts of the 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 and 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 with Sec. 188. Further Disclosed RPTs entered as follows:

Transaction	**The explanation provided by the Respondent**
Interest recd. From RPs	The company benefitted by pooling of resources as interest is charged at the 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 comments and are fully disclosed in financial statements

Transaction	The explanation provided by the Respondent
Remuneration drawn by MD	No violation of Sec. 188 as there is a different section which governs remuneration and therefore co. is fully Compliant It is in compliance with the provisions of the Companies Act and authorized 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 beneficial to the 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 with the provision of the Companies Act and authorized by the Board
Rental Income – Partnership	Name Board of Sri Rubber Industries was placed at the warehouse of respondent 1 company for 12 years, but no activity was done at the warehouse, and the Name board was only kept for sales tax purpose – there was a namesake agreement which was signed incidentally by 2nd respondent The said Arrangement was made many years ago and is well known to all stakeholders in the RBG family group
Rental Income – RBG Trading	Rental income due disclosed in the Balance sheet. Further respondents denied to pay rental income of 36 lakh as payment is made by way of commission for the use of premises The arrangement was made many years ago and is well known to all stakeholders in the RBG family group

- It was stated that MBP-1 disclosing interest was available for all directors except one director, who is the 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 the 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 the public domain
- The appointment of MD is in full compliance with the provision of articles and in compliance with the provisions of the Act. Further 203 is not applicable to the respondent companies.
- All RPTs are commercial transactions that benefitted the company and carried in the interest of the Company, and all allegations 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 exemptions under sections 185 and 188 of the Act based on an erroneous interpretation of exemptions granted to Private Companies under MCA notification dated June 5, 2015.
- The exemption will be applicable to a private company **only if the interest of its 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 the said notification.

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

- AOA is an 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 trustees on behalf of Company in a fiduciary capacity.
- It is found that AGM of companies has not been held. AGM gives an opportunity to shareholders to know the condition of the Company and also make a 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 had violated provisions of AOA.

Issue No. 3- Whether there is a 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 the Board of Directors and the shareholders, wherever applicable, were not obtained for entering into RPTs, and the 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.

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