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# CORPORATE LAWS

## Case Law Update

**Invesco Developing Markets Fund (Appellants/Invesco) versus Zee Entertainment Enterprises Limited (Respondent Company/Zee) Bombay High Court Order dated March 22 2022.**

**Facts of the case**

- Zee is a public limited and listed company. It is a well-known media enterprise. **Invesco holds about 17.88% of Zee's equity**. Zee's promoter and promoter group hold or control about 3.99% of Zee's equity shareholding.
- Invesco issued the **Requisition Notice on September 11 2021,** signed by requisite shareholders (>10%) and delivered to Zee's registered office for **9 items, the first 3** being for **the removal of the company's Managing Director (Mr. Goenka) and 2 other directors** and the **remaining 6** were related to the **appointment of 6 new Independent Directors (IDs) subject to approval** from Ministry of Information & Broadcasting **(MIB)**.
- As per Sec. 100 of Companies Act, 2013 ("CA, 2013"), **Zee's Board** would have had 21 days' time, i.e**. up to October 3, 2021, to convene the requisitioned Extraordinary General Meeting (EGM)**.
- On **September 29 2021**, **Invesco filed Company Petition** before the NCLT under Sec. 98(1) and 100 of CA, 2013 and sought relief. That matter before the NCLT is pending following an order of the NCLAT. Petition filed to **order to call and hold an EGM of Zee on or before October 28, 2021.**
- On September 30, 2021, the NCLT directed Zee to consider the Requisition and listed the NCLT Petition for hearing on October 4, 2021.
- On September 30, 2021, Zee's Board considered various legal opinions received and concluded that the Requisition was invalid/illegal and, accordingly, recorded its inability to convene the EGM in the best interests of Zee and its shareholders.
- On October 1, 2021, Zee emailed the Investor conveying the Board's rejection decision for the Requisition, citing multiple legal infirmities contained in

the Requisition. Zee brought a suit on October 1 2021, seeking an injunction against the Appellants from taking any action or step in furtherance of the Requisition.

- The Learned (Ld.) Single Judge granted an injunction restraining the Appellants from taking any action or step in furtherance of the Requisition including calling and holding an EGM under Section 100(4) of the Act.
- Aggrieved by the order passed by Ld. Single Judge, Invesco filed an appeal on October 28, 2021

**Question for consideration in Appeal:**

***Question 1***
Whether or not the learned Single Judge was correct in restraining the shareholders of Zee Entertainment Enterprises Limited from calling for and holding an EGM General Meeting as requisitioned by them.

***Question 2***
The alleged illegalities in the resolutions proposed under the aforesaid Requisition.

**Arguments on the part of Appellants**
The Ld. Councils on behalf of Appellant had submissions as follows:

- That a Civil Court cannot entertain a Suit of the nature filed by Zee;
- That the Ld. Single Judge's findings that this Court has jurisdiction to entertain the Suit is in the teeth of Section 430 of the Act which ousts the jurisdiction of Civil Courts regarding matters that fall within the domain of the NCLT;
- That since the Appellants had already filed an application under Section 98 i.e. the NCLT Petition, it is only the NCLT that is empowered to decide whether or not to call, hold or conduct a meeting;
- That this Court cannot interfere with the statutory right of a shareholder to call for an EGM. In support quoted a Supreme Court judgement ***LIC vs. Escorts & Ors. 1 (1986) 1 SCC 264***
- That strictly without prejudice to the aforesaid submissions, the Ld. Single Judge erred in finding that the requisitions proposed by the Appellants in the Requisition are illegal.

**Arguments on the part of Respondents**
- The jurisdiction of a Civil Court to entertain a challenge to the Requisition issued under Section 100 of the Act as being invalid/illegal/contrary to law is not affected by the bar contained in Section 430 of the Act
- The bar in Section 430 would be applicable only if the Act or any other law specifically empowered the NCLT to deal with and determine a particular matter.
- A suit impugning the legality and validity of a requisition issued under Section 100 and a requisitionist's right to call and hold a meeting pursuant to such requisition does not fall within the purview of Section 98 of the Act or attract the bar under Section 430 of the Act.
- The jurisdiction of the Court to entertain a suit impugning the legality

of a requisition purported to be issued under Section 100 of the Act, flows from the Civil Court's plenary jurisdiction/power under Section 9 of the Code of Civil Procedure, 1908 ("CPC") to try all suits of a civil nature [excepting suits, of which the cognizance is barred], including claims regarding the validity/legality of matters relating to/arising out of the provisions of the Act.

- Also placed reliance on the decisions in Isle of ***Wight Railway Co vs. Tahourdin, Queensland Press Ltd vs. Academy investments No. 3 Pty Ltd.*** and ***Rose vs. McGivern and others*** to submit that Courts have affirmed the power and jurisdiction of Courts to restrain a requisition calling for a general meeting if the object of the requisition is to do something which cannot be lawfully effectuated.

**Held**

- On a plain and literal reading of Section 100(4), the words "valid requisition" appear to mean numerical and procedural compliance and nothing further. In support of this interpretation, the reliance was placed on judgement ***Cricket Club of India vs. Madhav L. Apte***[1].
- Further stated that while dealing with the question of Jurisdiction of the Court in restraining the shareholders from convening EGM, the Court observed that they were unable to appreciate where the Act, its provisions pertaining to listed companies, and more particularly Sections 98 and 100 thereof would enable it to deviate from the ratio laid down in ***LIC vs. Escorts***. The Ld. Single Judge has not analyzed the facts, submissions and findings rendered by the Supreme Court in ***LIC vs. Escorts*** while cursorily accepting the submission of Ld. Council on behalf of the respondent company that in LIC vs Escorts, the debate was about mala fides and not about the legality or legal effectiveness of resolutions proposed at an EGM.
- Despite being placed before Supreme Court in ***LIC vs. Escorts***, the decision was taken in *Isle of Wight,* where it is held that If the object of a requisition to call a meeting were such, that in no manner and by no machinery could it be legally carried into effect, the directors would be justified in refusing to act upon it." The Supreme Court expressly held that a shareholder could not be restrained from calling a meeting, such shareholder need not disclose reasons for the resolutions proposed and that the reasons for the resolution are not subject to judicial review.
- In view thereof, notwithstanding the view adopted in the Isle of Wight, we see no occasion to deviate from the law stated in ***LIC vs. Escorts*** and adopt the view in Isle of Wight, which even the Supreme Court refused to do in ***LIC vs. Escorts***.

1. [1975] 45 Comp Cas 574 (Bom)

- Further, another distinguishing factor is that in the Isle of Wight, the Court was dealing with and interpreting Section 70 of the Companies Consolidation of Clauses Act, 1845, which provided for a requisition to "fully express the object of the meeting to be called." As opposed to this, there is no such requirement under Indian law.
- The Court held that we would not deviate from the law prevalent in India and follow the aforesaid view.
- We have no quarrel with the proposition that the NCLT is not a Civil Court nor with the proposition that the NCLT can exercise only such powers within the contours of jurisdiction prescribed for it. But these findings cannot by themselves be extended to mean that a Civil Court can grant an injunction to the calling or holding of an EGM in the teeth of settled law.
- Reliance placed by respondents on the decisions in ***Santosh Poddar vs. Kamal Kumar Poddar***[2] and other judgements is collectively distinguishable for the simple reason that in all of these decisions, the impugned resolution in question had already been passed. In the present case, Zee seeks an injunction from calling and holding an EGM in respect of resolutions that may or may not be passed. Such injunction, as has been repeatedly held, cannot be granted.
- Also highlighted resultant consequences which may arise should we rule that a Civil Court can, in certain cases, grant an injunction restraining shareholders of a company from exercising their statutory right to call for and hold an EGM.
- If we were to accept the proposition of Ld. Counsel of Respondent, not only would that be a clear departure from the law stated by the Supreme Court, but we would undermine the very foundations of corporate democracy in India.
- In the present case itself, the Appellants, being shareholders of Zee, have been unable to call for and hold an EGM despite the Requisition being addressed as early as September 11, 2021. We cannot lay down a precedent resulting in such drastic consequences derailing the democratic functioning of Companies across India owing to the non-cooperative and obstructive conduct of the Board of Directors.
- Further dealing with the second issue, i.e., alleged illegalities in the resolutions proposed under the Requisition, the Court observed that the power is given to shareholders of a Company by Section 160 and, more importantly, the proviso thereto, cannot go unnoticed. Therefore, according to the Ld. Single Judge, the fate of all directorial appointments must

2. 1992 SCC OnLine Bom 151

rest in the hands of the Nomination and Remuneration Committee (NRC) and the existing Board. In effect, The Ld. Single Judge has obliterated Section 160 of the Act. According to us, Section 160 does not make any distinction whatsoever between an Independent Director or otherwise. On a plain reading of Section 160, a shareholder of a Company clearly has the right to propose the appointment of an Independent Director.

- The Court further observed that we use settled principles of statutory interpretation to harmonize the various aforesaid Sections of the Act. Undoubtedly, a duty has been cast on the Board under Section 146(6) to opine on the integrity, expertise and experience of an Independent Director. Now, once the Board of Zee has received a requisition proposing the appointment of Independent Directors, we are unable to see the embargo on the Board to furnish their opinion in terms of Section 146(6).
- If we interpret Section 178(2) of the Act as Zee asks us to, a shareholder of a listed company would not only be disabled from proposing Independent Directors, but such disability would extend to all other Directors. Effectively, even a majority shareholder of a listed Company cannot suggest/appoint a Director without identification by the NRC. We do not think this is the intent or purpose of the Act and, more particularly, Section 178 thereof.
- For all of the reasons aforesaid, we conclude that the proposed resolutions contained in the Requisition are neither illegal nor incapable of being lawfully implemented and, consequently, setaside all of the Ld. Single Judge's findings in this regard on all counts.

*Note*: **The Summary on *Zee Entertainment Enterprises Ltd. vs. Invesco Developing Markets Fund,* Bombay high court (Single Judge) order dated October 26 2021, is published in the December issue of CTC Journal.**

**SEBI Adjudication order in the matter of Acropetal Technologies Ltd in respect of M/s K. Gopalkrishnan & Co (Statutory Auditor)**

**Facts of The case**

Acropetal Technologies Limited (hereinafter referred to as "**ATL**"/"**Company**") came out with an Initial Public Offer (hereinafter referred to as "**IPO**") for the issue of 1,88,88,889 equity shares of face value ₹ 10/- each at a price of ₹ 90/- per share, aggregating to ₹ 170 Crore during February 2011. Securities and Exchange Board of India (hereinafter referred to as "**SEBI**") took up the preliminary investigation in the IPO of Acropteal Technologies Limited to ascertain whether there were *inter-alia* any violation(s) of the provisions of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003 (hereinafter referred to as "**PFUTP Regulations**") with regard to the bidding process, examination of disclosures made by the company in the offer documents/ prospectus and deviations from objects of the issue if any and examination of fund flows from IPO proceeds.

SEBI found that on page 64 of the prospectus of ATL, it was disclosed that ATL had taken

a bridge loan of ₹ 20 crore, out of which ₹ 7 crore was used towards construction of building and remaining, towards working capital. SEBI further highlighted that ATL, vide its letter dated May 2, 2016, had informed that the said amount of ₹ 7 crores was transferred to M/s Equastone Properties Pvt Ltd (hereinafter referred to as 'Equastone') as an advance towards the construction of software development centre. SEBI highlighted that ATL had further submitted that said project was cancelled, and ATL received back the advance paid to Equastone. SEBI submitted that from the bank account statements of ATL, it was observed that the remaining ₹ 13 crore was transferred abroad, for which no reason whatsoever could be provided by ATL. Hence, it is observed that the entire transaction was not genuine and disclosure as appearing in the prospectus was false. SEBI further stated that M/s. Gopalakrishnan & Co. (**"Noticee"**), being a statutory auditor of the company, had certified, vide letter dated January 24, 2011, that the loan amount was utilized as follows:- (a) Advance towards the construction of building - ₹ 7.00 Cr (b) Towards working capital - ₹ 13.00 Cr. SEBI further submitted that vide letter dated August 10, 2016, Noticee was advised by SEBI to provide basis/ rationale for certifying the aforementioned transactions relating to utilization of bridge loan. The Noticee vide his reply dated August 20, 2016, stated that they have given the certification based on the document made available by the ATL for verification.

SEBI also highlighted that apart from ATL, the Noticee was the auditor for Equastone Properties (to whom ₹ 7 crores of the bridge loan amount was transferred) also at relevant point in time and hence, it is alleged that it is unlikely that the Noticee was unaware of the connection between ATL and Equastone and the genuinity of the transactions.

Based on the observations, SEBI alleged that the Noticee had wrongly certified the utilization of the bridge loan amount of ₹ 20 crore in the prospectus of ATL. The certification provided by the Noticee was part of the prospectus of ATL. Hence, the prospectus of ATL contained misleading information relating to the bridge loan, which was based on the certificate provided by the Noticee.

**Charges levied**

In view of the above, it is alleged that the Noticee, Statutory Auditor of ATL, had wrongly certified the utilization of bridge loan amount of ₹ 20 crore in the prospectus of ATL and violated regulations 3(b), (c), (d), 4(1), 4(2), (f), (k) & (r) of PFUTP Regulations.

**Arguments by Appellant**

**Certification of Bridge Loan of ₹ 20 crores was based on the representations made by ATL, the books of account and other documents and information submitted by ATL**

Noticee submitted that the role of an auditor is limited to exercising reasonable care and skill, he is not bound to perform any act outside the scope of his ordinary duties to detect fraud. Noticee further submitted that certification was based upon the assurances of the Board of Directors, promoters, and management regarding the utilization of the bridge loan. Noticee stated that he was informed by the Company that INR 7 Crore, out of the entire loan amount, shall be used for the construction of a software development centre. The Noticee verified the claims of the company by examining the

agreement dated March 15, 2011, between the Company and Equastone for the construction of the software development centre. The Noticee relied upon Clause 2.1 of the said agreement, which stated that the company shall pay an advance sum of INR 7 Crores to Equastone for the construction of a software development centre in Bangalore and provided his certification accordingly. Noticee further argued that it is not SEBI's case that such amounts have not been transferred to Equastone, thereby making the certification incorrect. In relation to the remaining amount of the bridge loan, i.e., INR 13 Crore, the auditor was informed by the company stated that the same was used toward working capital. Noticee corroborated the company's representations with the General Ledger of the Company for the financial year 2010-2011 and the Form A2 submitted by the Company to United Bank of India. Noticee further submitted that he was informed that the company had identified scope for huge business in the Middle East, Europe and the US and were exploring the potential markets there. With this background, expenditure towards working capital did not seem out of the ordinary at the relevant time.

Noticee further highlighted that the supporting documents showed that remittances had been made by the company towards onsite expenses and other working capital requirements to the extent of around INR 6 crore. Further, the remainder amounts were utilized towards the purchase of software, repayment of the loan, etc. In view of this, the Noticee humbly submitted that he took all measures necessary to verify the representations of the company and only provided the certification on the satisfaction that the remittances are made through normal banking channels and have been recorded adequately as working capital expense in books of account.

The Noticee further submitted that he could not be held liable for violating the PFUTP Regulations since he had no reasonable grounds to believe that the representations made by the company were false and fictitious. The Noticee submitted that he exercised reasonable care and caution while examining the prospectus and certifying it and ought not to be penalized for the alleged fraud by the company. Noticee further alleged that he has been equally a victim of fraud as the general public.

**Arguments by SEBI**

**Certification of Bridge Loan of ₹ 20 crores was based on the representations made by ATL, the books of account and other documents and information submitted by ATL**

SEBI stated that **the** prospectus was dated February 25, 2011, and the said agreement was dated March 15, 2011. SEBI further stated that Noticee had certified vide letter dated January 24, 2011, that the loan amount was utilized till January 21, 2011, as follows:— (a) Advance towards the construction of building - ₹ 7.00 Cr (b) Towards working capital - ₹ 13.00 Cr. SEBI highlighted that no date of payment of advance made to Equastone by ATL was mentioned in the agreement and the fact that the agreement date was of later date than the prospectus date, and that Noticee has not perused the same during certifying the utilization of Loan amount on January 24, 2011. SEBI further highlighted that except for submitting an agreement, no other supporting documents, viz., correspondences prior to and post

execution of agreement, board resolution, reason and communication of cancellation etc., were furnished neither by ATL during the investigation to strengthen its submission that ₹ 7 crores which was transferred by ATL to Equastone was for the construction of a software development centre in Bangalore nor by the Noticee.

SEBI further submitted that the Noticee had perused the Copy of the General Ledger of ATL for the (FY) 2010-11 showing accounting entries in respect of the advance of ₹ 7.00 Crores to Equastone Properties Private Limited. But SEBI stated that financial statements for the period 2010-11 were adopted and approved by the Board of Directors of the Company at their meeting held on August 12, 2011, and were adopted and approved by the shareholders at the Tenth Annual General Meeting held on September 28, 2011. But all these documents were adopted and approved at a later date than the prospectus date and said certification date. With respect to utilization of bridge loan of INR 13 Crore, SEBI stated that Noticee relied upon the statements and documents provided by ATL. SEBI noted that there was no seal of the bank on the Copies of Form A2 submitted by ATL to United Bank (Authorised Dealer) for making the said overseas remittances. Further, it was not supported by bank account statements but was supported only by General Ledger of ATL for the (FY) 2010-11 showing accounting entries in respect of overseas remittances of ₹ 13.00 Crores, made towards onsite expenses of working capital. SEBI further highlighted that Noticee was also the statutory auditor of Equastone for the FY 2010-11 & 2011-12, i.e. during the period, ATL came out with an IPO. Thus, in view of the aforesaid, SEBI claimed that Noticee miserably failed to identify and verify the correctness in the utilization of bridge loan despite being associated with ATL for a long period, i.e., from 2001 till 2017 and also being a statutory auditor of Equastone during the time, ATL made an IPO. SEBI also claimed that the Noticee has not demonstrated in his reply as to whether independent confirmation was made by Noticee. Considering the materiality and the magnitude of the bridge loan and the seriousness of the Public issue made by ATL, the auditor should have at least carried out some independent assessment based on documents other than the statements provided by the company. SEBI further noted that Noticee had not brought any evidence to show in the instant proceedings and during the investigation that it had provided the said certificate with due diligence and care and that he had raised all possible queries expected to be raised by any prudent auditor to the management in the normal course of his work. SEBI, hence stated that the Noticee it has blindly accepted the documents and statements provided by ATL.

SEBI further stated that it had been alleged that, Noticee had violated regulations 3(b), (c), (d), 4(1), 4(2), (f), (k) & (r) of PFUTP Regulations by wrongly certifying the utilization of bridge loan amount of ₹ 20 crore in the prospectus of ATL. SEBI also stated that to establish the charge of fraud against Noticee in the instant proceedings, and there is nothing on record to find that the Noticee has connived or colluded with ATL or its directors, in the absence of which, SEBI stated that it is of the view that there is no deceit or inducement by the Noticee. Undoubtedly an auditor is duty-bound to be absolutely and completely diligent

and cautious while preparing, signing and certifying Annual Accounts and/or any other Audit report. However, in view of the aforesaid findings, wherein it is seen that adequate/proper documents were not submitted by ATL during the investigation, it casts a shadow of doubt on the documents submitted by the company to the Noticee. Further, Regulation 60(7)(a) of Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009, places the onus on the Issuer company to make true and fair disclosure in any advertisement caused to be issued by the Issuer. Moreover, no material or evidence sufficient enough has been brought on record to show why the transaction with Equastone would have raised red flags for, especially when the money was transferred to Equastone. Therefore, in the absence of any material available on record, the charge of fraud or collusion or connivance with the ATL and directors of the company cannot be levied on the Noticee, only on the ground that he was not diligent or cautious or did not check the utilization of bridge loan through other sources. SEBI was of the view that aforesaid lack of due diligence can only lead to professional negligence, which would amount to a misconduct which could be taken up only by the Institute of Chartered Accountants of India.

**Held**

Matter disposed off without penalty.

**Cases referred**

**SEBI:** ***HSBC Securities (India) Pvt Ltd vs. SEBI [Appeal no. 99/2007]*** – Order dated: February 20, 2008, order of the Whole Time Member dated June 29, 2021, in respect of Saffron Capital Pvt Ltd (Merchant banker to this IPO) in the matter of ***Acropteal Technologies Ltd., Price Waterhouse Coopers vs. SEBI*** [SAT order dated: September 9, 2019], Hon'ble Bombay High Court in Writ Petition no. 5249 of 2010 (filed by Price Waterhouse, Bangalore) and Writ Petition no. 5256 of 2010 (filed by 10 CA firms along with their partners) dated: August 13, 2010.

**Noticee:** ***V. Natarajan vs. SEBI*** [Appeal no. 104 of 2011, SAT order], ***Brooks Laboratories Ltd vs. SEBI***, March 21, 2018, HSBC Securities and ***Capital Markets (India) Private Ltd vs. SEBI,*** February 20, 2008.

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"Books are infinite in number and time is short. The secret of knowledge is to take what is essential. Take that and try to live up to it."

— *Swami Vivekananda*