CS Makarand Joshi

CORPORATE LAWS
Case Law Update

SEBI Order - 1

Order of Adjudicating Officer of Securities and Exchange Board of India

Name of the Case: In the matter of IZMO Ltd.

Facts of the case

1. Securities and Exchange Board of India ('SEBI') conducted an examination in the matter of M/s. IZMO Limited (hereinafter referred to as "IZMO" or "Noticee" or "Company"), a company having its shares listed on BSE Ltd. ('BSE') and National Stock Exchange of India Ltd. ('NSE'), based on a reference received from Economic Offences Wing (EOW) with regard to a complaint of Shri Samarth Khullar dated February 03, 2020 ("the complaint"), on behalf of 25 persons, against IZMO, M/s Hughes Precision Manufacturing Pvt. Ltd ("HPMPL") and their directors, KMPs, statutory auditors, etc., to ascertain whether there was any violation of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 ("LODR Regulations") and the circulars issued thereunder by the Noticee.

2. On investigation, SEBI observed that the Noticee had made a misstatement in its Annual Report for the Financial Year 2017-18 and its disclosure dated September 26, 2018, made to the Stock Exchanges. IZMO in its Annual Report for the Financial Year 2017-18, stated that *"...Izmo is entering the defense manufacturing sector through its subsidiary, Hughes Precision Pvt. Ltd...."* In this regard, it is alleged that the said disclosure is a misstatement, as HPMPL was not a subsidiary of IZMO. SEBI gathered that HPMPL is not a subsidiary of Noticee from the disclosure of the Noticee dated September 26, 2018.

3. IZMO, in its disclosure dated September 26, 2018, to the Stock Exchanges had stated that *"....IZMO Ltd., under its (proposed) wholly owned subsidiary company, M/s Hughes Precision Manufacturing Ltd. is pleased to announce that the*

Company has received the license to Manufacture and Proof Test Military Calibre Ammunition...." On perusal of this, it was alleged that the said disclosure read with the rest of the disclosure appears to be misleading as it is unclear who has received the license, i.e., IZMO or HPMPL. SEBI further alleged that Noticee in its disclosure dated September 26, 2018, had inter alia stated that HPMPL would become a wholly owned subsidiary of IZMO Ltd, which is not in tandem with disclosures in the annual report for FY 2017-18. Further, it was observed that the Noticee did not raise funds through Qualified Institutional Placement (QIP) as approved in its Annual General Meeting held during September 2018. However, Noticee's decision to delay its plan for entering the defense business through HPMPL was not communicated to the investors. SEBI alleged that since the Noticee had disclosed that HPMPL would become a wholly owned subsidiary of the Company, it should have intimated the updates on the same regarding the aforesaid delay. Therefore, it was alleged that the Noticee had violated Regulation 30(7) of LODR Regulations read with Clause 2(i) of the Listing Agreement and for wrong disclosure in the annual report for FY 2017-18 the Noticee has violated Regulation 4(1)(c) and 4(1)(h) of the LODR Regulations read with Clause 2(i) of the Listing Agreement.

Charge

Violation of Regulation 4(1)(c), Regulation 4(1)(h) of the LODR Regulations, and Regulation 30(7) of LODR Regulations read with Clause 2(i) of the Listing Agreement.

Arguments/submissions by Noticee

1. **Mis-statement in the annual report for FY 2017-18:** In this regard, Noticee admitted that Hughes Precision Manufacturing Pvt. Ltd. (HPMPL) is not a subsidiary of IZMO Ltd. and was proposed to be a wholly owned subsidiary of the Company. Still, the word 'proposed' was inadvertently missed out before the word 'subsidiary.' Therefore, the said misstatement in its Annual report for the Financial Year 2017-18 suffers from nothing more than an inadvertent error/omission, which cannot be termed as a misstatement and therefore denied having violated regulation Regulations 4(1)(c) and 4(1)(h) of the LODR Regulations read with Clause 2(i) of the Listing Agreement.

2. **Disclosure of receipt of license by 'proposed' subsidiary is misleading:** As regards its misleading statement in its disclosure dated September 26, 2018, to the stock exchanges, the Noticee stated that the bare perusal of the said disclosure brings out the fact that IZMO was planning a diversification into defense vertical through its proposed subsidiary company viz., HPMPL. Further, it also stated that the disclosure was made by IZMO only to keep the stock exchanges and investors abreast of the developments. Further, the Noticee stated that the object clause in the Memorandum of Association of IZMO does not permit it to enter into defence-related activities. Further, IZMO had not amended the object clause of the memorandum. Therefore, any act beyond the objects of the MOA is ultra-vires and void. Therefore, it

cannot be assumed that IZMO was granted the license to manufacture and proof test military calibre Ammunition under the Arms Act, 1959, and the Arms Rules, 2016. Thus, it cannot be said that the disclosure made by IZMO on September 26, 2018, is misleading, and it is crystal clear that HPMPL had received the license. Therefore, it denied having violated Regulations 4(1)(c) and 4(1)(h) of the LODR Regulations read with Clause 2(i) of the Listing Agreement.

3. **Delayed disclosure that HPMPL would become a subsidiary:** As regards the allegation of delay regarding disclosing that HPMPL would become its wholly owned subsidiary, the Noticee stated that the plan to have HPMPL as its wholly owned subsidiary was not discarded but only deferred. The company has always kept its stakeholders updated about the developments regarding its intentions and projects to enter into the defense sector. The same was evident from the 'notes' section of the Corporate Announcements(s) regarding the outcome of the Board Meeting. Therefore, it denied violating the provisions of Regulation 30(7) of the LODR Regulations read with Clause 2(i) of the Listing Agreement.

Arguments by SEBI

1. **Misstatementent in the annual report:** In this regard, SEBI stated that Noticee did not have any subsidiary at the relevant point of time to make such a statement in the annual report. This establishes that the statement made in the annual report was a misstatement. Besides, irrespective of whether HPMPL was a "proposed subsidiary" or an actual "subsidiary," the statement, i.e., *"Izmo is entering the defense manufacturing sector through ..... Hughes Precision Pvt. Ltd."* by itself is sensitive enough to materially affect the price of the securities of the Noticee Company since the moment it was decided and used the Name of Hughes Precision Pvt. Ltd., by IZMO. Such information provided by a listed company is deemed to be price sensitive information ('PSI') in terms of the definition as per Regulation 2(ha) of PIT Regulations, 1992, the moment it came into existence since it has the potential to deceive prospective investors. SEBI further stated that as per Clause (c) of sub-regulation 1 of regulation 4 of the LODR Regulations, listed entities are required to refrain from misrepresentation and ensure that the information provided to the stock exchanges and investors are not misleading. As per Clause (h) of sub-regulation 1 of Regulation 4 of the LODR Regulations, the listed entity is required to make specified disclosures and follow its obligations in letter and spirit taking into consideration the interest of all stakeholders. SEBI observed that the said statement is solely a misstatement by the Noticee, which is in direct conflict with the essence of the principles governing the disclosures and obligations as it had wrongly represented a certain vital piece of information to the public i.e. wrongly stating that HPMPL was its subsidiary when in reality it wasn't. SEBI highlighted that, since the Noticee

is casting aside its responsibilities that the law is aiming to ensure, the contention of the Noticee is not at all acceptable that an inadvertent error/omission, cannot be termed as a misstatement and find that its submissions in this regard do not contain any merit. Hence it is clear that Noticee has violated Regulations 4(1)(c) and 4(1)(h) of the LODR Regulations read with Clause 2(i) of the Listing Agreement.

2. **Disclosure of receipt of license by 'proposed' subsidiary is misleading:** SEBI stated that contention of the Noticee that, a bare perusal of the disclosure given on September 26, 2018 brings out the fact that IZMO was planning a diversification into defense vertical through its proposed subsidiary company *viz*., HPMPL, is not acceptable. In this regard, SEBI stated that it does not specify whether it is IZMO or the wholly-owned subsidiary, which received the license and therefore, it is ambiguous and vague. Further, as regards the Noticee's statement that the said disclosure was made by IZMO only to keep the stock exchanges and investors abreast of the developments, SEBI submitted that it is important to note that clear and unambiguous disclosures of the relevant information by companies are essential for maintaining transparency about the affairs of the company which helps elimination information asymmetry. Therefore, the Noticee's argument in this regard is without any merits. SEBI highlighted that the Noticee also stated that the object clause in the Memorandum of Association of IZMO does not permit it to enter in defence-related activities and therefore, any act beyond the objects of the MOA is ultra-vires and void. Therefore, it cannot be assumed that IZMO was granted the license to manufacture and proof test military calibre Ammunition. In this regard, SEBI submitted that it never assumed such a stand that IZMO was granted the license to manufacture and proof test military calibre Ammunition. It was always SEBI's case that the statement of the Noticee was unclear and misleading. Accordingly, the Noticee's submission in this regard is devoid of merit. Therefore, SEBI said that the Noticee had violated Regulations 4(1)(c) and 4(1)(h) of the LODR Regulations.

3. **Delayed disclosure that HPMPL would become a subsidiary:** SEBI stated that Regulation 30(7) of the LODR Regulations requires all the listed entities to make disclosure updating material developments regularly, until the event is resolved/closed with relevant explanations. In the current case Noticee's plan to have HPMPL as its wholly-owned subsidiary was only deferred as understood from its reply. However, one cannot overlook that the deferment is also material development that needs to be updated regularly in the form of disclosures. Since, the Company had failed to update the relevant the details of the deferment in its plan to have HPMPL as its wholly-owned subsidiary, the argument of Noticee that it always kept its stakeholders updated about the developments regarding its intentions and projects to enter into the defense

sector cannot be accepted. Therefore, there is no merit in the Noticee's argument in this regard, and it is found that it has violated Regulation 30(7) of the LODR Regulations read with Clause 2(i) of the Listing Agreement.

Hence it is clear that Noticee has violated Regulations 4(1)(c), 4(1)(h), and 30(7) of the LODR Regulations read with Clause 2(i) of the Listing Agreement.

Penalty

As per Section 23-I of the SCRA read with Rule 5 of SC(R) Rules, a penalty of ₹ 5,00,000/- (Rupees Five Lakhs Only) was imposed on the Noticee, in terms of the provisions of Section 23E of the Securities and Exchange Board of India Act, 1992.

Cases quoted by Noticee: Nil

Cases quoted by SEBI: ***Ranjan Varghese vs. SEBI (Appeal No. 177 of 2009 and Order dated April 08, 2010), Appeal No. 66 of 2003 – Milan Mahendra Securities Pvt. Ltd. vs. SEBI, Coimbatore Flavors & Fragrances Ltd. vs. SEBI (Appeal No. 209 of 2014 order dated August 11, 2014)***

SEBI Order - 2

Order of Adjudicating Officer of Securities and Exchange Board of India

Name of the Case: In the matter of Securekloud Technologies Ltd and in respect of Securekloud Technologies Ltd, Mr. Gurumurthi Jayaraman, Ms. Padmini Ravichandran, and Mr. G. Sri Vignesh

Facts of the case

A. Practicing Company Secretary ("PCS") viz. M/s P. Sriram & Associates of M/s Securekloud Technologies Limited (the Company/Noticee No. 1) made observations, inter alia, of not following due process for approval of Related Party Transactions (RPTs), Independence of Independent Directors (IDs) in the company, Non-consolidation of accounts of certain companies in the accounts of M/s Securekloud Technologies Limited and other non-compliances in terms of disclosures to be made to the Committees and Board as contemplated under Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 (hereinafter referred to as "SEBI LODR Regulations 2015") in the certificate on compliance with conditions of Corporate Governance for FY 2018-19, issued under Regulation 34 (3) of SEBI LODR Regulations, 2015. Additional facts peculiar to each allegation are quoted below:

B. **Not following due process in respect of related party transactions:** As per the Annual report for FY 2018-19, the Statutory Auditor of the Company, M/s Deloitte Haskins & Sells made certain observations stating that, "*In the absence of appropriate processes for identifying related parties they would be unable to comment on the accuracy and completeness of the related parties identified and disclosed by the Company including compliance with obtaining necessary approvals, as required, from those charged with governance*". In addition to this, the PCS, in the certificate of compliance issued in the Annual Report for FY 2018-19 for the Company, has inter-alia stated as

follows, *"The company has entered into certain Related Party Transactions without taking prior approval of the Audit Committee and Board as required under SEBI (Listing Obligations and Disclosure Requirements), Regulations, 2015"* In this regard, SEBI advised PCS to provide details of non-compliance with regard to approval process of RPTs. The PCS, *vide* email dated June 08, 2021 *inter-alia,* specified the following: *"Many transactions reported in the Balance sheet under related parties did not find place in the Minutes of Audit Committee Meetings, which included payment of remuneration to Mr. Ravichandran Srinivasan (relative of Independent Director, Ms. Padmini Ravichandran), payment of salary to ID Mr. Gurumurthy Jayaraman, transaction with Sustainable Certification (India) Private Limited. The company had also provided ad-hoc approvals to transactions with subsidiaries without specifying the names of subsidiaries."* Further the Company provided to SEBI relevant minutes of audit committee meetings held for the year 2017-18 and 2018-19 wherever approvals for RPTs were granted. Further comments of the audit committee of the Company were sought by SEBI. SEBI further vide email dated July 30, 2021 raised queries to aforesaid Independent Directors regarding the details of all RPTs entered into by the company in FY 2017-18 and FY 2018-19 along with details of prior approval by Audit Committee and approval by shareholders in case of material RPTs. Aforesaid Independent Directors (excluding Mr. Biju Chandran) vide emails dated August 02, 2021 and August 06, 2021 provided details of the RPTs executed in FY 2017-18 and FY 2018-19 along with the dates on which the Audit committee provided its approval. The Audit Committee members also *inter-alia* mentioned the following: *"All the related party transactions have been disclosed in the Annual report for the FY 2017-18 and FY 2018-19 and prior approval of the Audit Committee has been obtained and since the transactions were within the specified limits, there was no requirement of Shareholders approval as per Reg. 23(4) of the LODR Regulations, 2015."* SEBI noted that Regulation 23(2) of SEBI LODR envisages that "prior approval" of Audit Committee shall be necessary for all RPTs. In the instant case, it was seen from the minutes of the Audit Committee for FY 2017-18 and FY 2018-19, that prior approval has been explicitly sought only for certain RPTs. For other transactions, no explicit approval from Audit Committee was neither observed in the minutes and nor has the company produced any other supporting document proving otherwise. Further, it was seen that few RPTs were ratified by the Audit Committee at a later date.

C. Non-consolidation of accounts of certain companies in the accounts of M/s Securekloud Technologies Ltd: In addition to the above facts quoted at point (A) above, following facts needs to be noted. Statutory Auditor of Noticee no. 1 observed that 3 entities (viz. 8K Miles Cloud Solutions Pte. Ltd., Singapore; 8K Miles Software Services Pte. Ltd., Singapore and 8K Miles Software Services UK Ltd,

UK) have not been considered by the Company as its subsidiaries. Further as per publicly disclosed information, M/s 8K Miles Cloud Solutions Pte. Limited, Singapore has stated itself to be a subsidiary of the Company. This entity was incorporated on May 8, 2017. Further, 8K Miles Software Services Pte. Ltd, Singapore and 8K Miles Software Services UK Limited, United Kingdom exist with the promoter directors appearing as shareholders/directors. Also incorporation of these wholly owned subsidiaries in these countries were approved by the Board of Directors of the Company in their meeting held on May 30, 2018. However, all these three entities have not been considered by the management of the Company as subsidiaries in their standalone financial statements. PCS also opined that the aforesaid 3 subsidiaries viz. 8K Miles Cloud Solutions Pte. Ltd., Singapore; 8K Miles Software Services Pte. Ltd., Singapore and 8K Miles Software Services UK Ltd, UK were neither disclosed as subsidiaries nor were their financials consolidated with that of the Company. Further, Companies House Database of Government of UK, showed Mr. Rama Subramani Ramani alias Mr. R S Ramani, who is the promoter of the Company, as director of 8K Miles Software Services UK Limited, United Kingdom. Based on this, the examination report stated that 8K Miles Software Services UK Limited is a related party of the Company. However, as per the filing dated April 30, 2019 with the Government of UK, it is seen that 8K Miles Software Services UK Limited is dormant and has equity value of GBP 1. Ind AS 24 pertaining to related party disclosures, states that it is appropriate to disclose the related party relationship when control exists, irrespective of whether there have been transactions between the related parties. In the instant case, it is clear that there exists a relationship between 8K Miles Software Services UK Limited, UK and Noticee no. 1, since as per filings with Company House UK, Mr. R S Ramani (promoter of the company) is the sole shareholder of M/s 8K Miles Software Services UK Limited. This relationship is not disclosed by the Company vide its annual reports or any other public disclosure. Hence, by not disclosing all its related parties, it was alleged in the SCN that the Company is in violation of Regulation 48 of SEBI LODR Regulations, 2015 which states that the listed entity shall comply with all the applicable and notified accounting standards from time to time.

Charge

Noticees *viz*. Securekloud Technologies Limited (Noticee No. 1) has violated the various provisions of SEBI LODR Regulations, 2015 and/or Securities Contracts (Regulation) Act, 1956 (hereinafter referred to as SCRA, 1956). Noticee No. 1 is a company listed at BSE/NSE.

Arguments/submissions by Noticee

A. Not following due process in respect of related party transactions was an inadvertent error: Noticee No. 1 submitted that it had inadvertently

missed to take prior approval of certain RPTs from Audit Committee as per Regulation 23 of SEBI LODR Regulations. Noticee No. 1 also referred to four RPTs (*viz*. ₹ 7.23 cr. with 8K Miles Software Services Inc. subsidiary, ₹ 2.03 cr. & ₹ 40.74 cr. with R S Ramani, Promoter, Director and 1.19 cr. with Mr. Suresh Venkatachari) that were subsequently ratified on February 14, 2018. Noticee also relied on Hon'ble Supreme Court judgment passed in the matter of ***National Institute of Technology ('NIT') and another vs. Pannalal Choudhury and Another (2015) 11 SCC 669*** to explain the expression 'ratification'. In respect of RPT to the tune of ₹ 0.55 cr. executed with Mr. Suresh Venkatachari, Noticee No. 1, in its reply, stated that it was an unsecured loan taken from Mr. Suresh Venkatachari and the same was taken in the best interest of the company to help the company meet its financial obligations. Further, Noticee No. 1, in respect of RPT of ₹ 13.95 cr. explained that the company had a working capital facility with IFCI for which personal assets of Suresh including 25,75,000 equity shares (8K miles) were placed as collateral. IFCI sold the pledged shares to realize the loan. Hence, the IFCI loan was replaced with Suresh's loan. So the need for prior approval of audit committee in the said instance did not arise. With respect to director remuneration paid to Mr. Suresh Venkatachari, Noticee No.1, in its reply, stated that no director remuneration was paid to Mr. Suresh Venkatachari from the Company. Rather, he was drawing remuneration only from the overseas subsidiary i.e. Securekloud Technologies Inc. Attention was brought to the relevant pages (140 & 206) of Annual Report for FY 2018- 19. Further, Noticee No. 1 submitted that appointment of Mr. Suresh Venkatachari and Mr. R S Ramani are governed by Sections 196, 197 and 203 of the Companies Act, 2013 read with Schedule V and all other applicable provisions and the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014 (including any statutory modification(s) or re-enactment thereof, for the time being in force) of Companies Act, 2013. Noticee No. 1 submitted that since the appointment of both Mr. Suresh Venkatachari and Mr. R S Ramani were approved by the Nomination and Remuneration Committee and the Board itself, there was no role of Audit Committee in respect of such transactions. Noticee No. 1, in its reply, stated that remuneration paid to Independent Directors viz. Gurumurthi Jayaraman, Padmini Ravichandran, Babita Singaram and Dinesh Raja Purmiamurthy are excluded from RPTs. Similarly, Noticee No.1 refuted that remuneration paid to KMPs falls in the category of RPT items specified in Section 188 (1) of the Companies Act.

B. Non-consolidation of accounts of certain companies in the accounts of M/s Securekloud Technologies Ltd as they were not dormant companies: Securekloud Technologies Ltd. Has not made any investment in 8K Miles Software Services PTE Ltd, Singapore, 8K Miles Software Services UK Limited,

United Kingdom and 8K Miles Cloud Solutions PTE Limited, Singapore. These Companies are not subsidiaries and no transactions have taken place with Securekloud Technologies Limited (formerly 8K Miles Software Services Limited). Therefore, there was no requirement to consolidate the same in the Company's accounts. In the context of IND AS 24, the Noticee No. 1, stated that as it had not invested any amount in the same company and as such there was no control. The said company was dormant company with equity value of just GBP 1 and never carried/started any business. Therefore, the Noticee No. 1 contended that there was no breach of IND AS 24 in the facts and circumstances of this case.

Arguments by SEBI

A. **Not following due process in respect of related party transactions was not an inadvertent error:** SEBI stated that crux of the allegations is that Noticee No. 1 had not obtained "prior approval" of the Audit Committee with respect to certain Related Party Transactions. These transactions include certain loan transactions to related parties; investments in related parties; generation of revenue from related parties including interest income; repayment of loan to related parties; sale of intangibles; remuneration/sitting fee etc. entered by the company with certain identified related parties during FY 2017-18 and 2018-19. It is to noted that Regulation 23(2) of SEBI LODR Regulations specifically mandates "prior approval of Audit Committee" for RPTs. SEBI highlighted that defense of the company that not obtaining "prior approval" is an inadvertent error, is not acceptable in light of the avowed object underlying the provisions. Likewise, the defense of 'ratification' set up by the company is of no avail, in this context. Judgment of the Hon'ble Supreme Court cited by the Noticee does not pertain to the realm of Companies Act and deals with "ratification" in a totally different context and in the general sense of the term. SEBI further stated that object of introduction of Audit Committee in the governance realm of listed entities and the norms mandating "prior approval of the Audit Committee" for RPTs are significantly different from the governance processes prescribed to be followed in an academic institute (NIT) which was pertaining to case quoted by Noticee no. 1. "Ratification" cannot be a general principle to be extended to defeat the explicit mandate of "prior approval" laid down in SEBI (LODR) Regulations, 2015 for related party transactions. Such RPTs have an impact not only on the investor's interest but also on the level of transparency required in corporate governance. Loans by the related parties advanced to the Company and loan advanced by related parties to the Company such as 8K Miles Software Services Inc. and 8K Miles Media Pvt Ltd etc required prior approval of Audit Committee. Loan transactions between the Company and R S Ramani, the promoter - director as well as the transactions with 8K Miles Software Services Inc. were substantial during the year 2017-18 constituting more than ₹ 85 cr. So, it is evident that there were substantial financial transactions between the company and the related parties, to the tune of close

to ₹ 100 cr. for the said two financial years, which were executed without the knowledge and/or obtaining the prior approval of the Audit Committee of the Company. Remuneration/sitting fees amounting to ₹ 4.06 cr. categorized as RPTs is not very significant and the same may not qualify as material RPT, as contended by the Counsel appearing for Noticee No. 1. Hence, Noticee No. 1, by having entered into substantial financial transactions with its related parties, without obtaining prior approval from Audit Committee, as admitted, has committed a violation of Regulation 23(2) of SEBI LODR Regulations 2015 and is liable for penalty.

B. Non-consolidation of accounts of certain companies in the accounts of M/s Securekloud Technologies Ltd as they were not dormant companies: SEBI stated that there is no material brought out in the examination report showing the association of 8K Miles Software Services PTE Ltd, Singapore and 8K Miles Cloud Solutions PTE Limited, Singapore with the company viz. M/s Securekloud Technologies Ltd. As regards 8K Miles Software Services UK Limited, United Kingdom, it is noted from the available records that Mr. R. S. Ramani who is the promoter of the Company, is also the director of 8K Miles Software Services UK Limited which is also evident from documents filed with Companies House, Government of UK. Further, SEBI noted that as on April 30, 2019 it is seen that 8K Miles Software Services UK Limited, has share capital of GBP 1. It is also seen that the documents filed with Companies House, Government of UK that 8K Miles Software Services UK Limited is a 'Dormant Account' and a statement was also mentioned in the Balance sheet that *"For the year ending April 30, 2019, the company was entitled to exemption under section 480 of the Companies Act, 2006 relating to dormant companies"*. Further, from the document filed with Companies House, titled as "Full details of Shareholders", it is seen that Mr. Ramani Rama Subramani is holding 1 share of 8K Miles Software Services UK Limited. Hence looking at all the evidences it can be inferred that sufficient material has not been brought out in the examination report to establish that 8K Miles Software Services, UK Limited is an active subsidiary of Noticee No.1. In view of the facts stated above, SEBI refused to accept that 8K Miles Software Services UK Limited is indeed a "subsidiary", of Noticee No.1 as per the provisions of the Companies Act, 2013**. Penalty under Notice no 1 ₹ 25,00,000, Notice no 2 – ₹ 10,00,000, Notice No 3 - ₹ 10,00,000 and Notice No 4 – ₹ 4,00,000.**

Penalty

Noticee name	*Violations*	*Penalty under provisions*	*Penalty*
Securekloud Technologies Ltd (Noticee no. 1)	Regulation 23(2), Regulation 17(1)(b), Regulation 18(1)(d), Regulation 20(2A) and Clause 17 of Para A of Part A of Schedule III read with Regulation 30(2) read with Regulation 4(1)(h) of SEBI (LODR) Regulations, 2015 and Section 21 of SCRA, 1956.	Section 23 E of SCRA, 1956 read with clause 2 of the Listing agreement	₹ 25,00,000

Co.'s Act Order - 1

In the matter of *Hamlin Trust & Ors. vs. Rattan India Finance Private Limited And Ors.,* NCLAT order dated 7th September 2022

Facts of the case

- Rattan India Finance Private Limited, (hereafter called as Rattan India) is a joint venture (JV) Non-Banking Financial Company (NBFC), and Hamlin Trust, (appellants) is 50% shareholder/JV partner in Rattan India along with Rose Investments ("Respondent").
- Due to a dispute between the Hamlin Trust and Rose Investments, the business operations of Rattan India were hampered, and as a result, both the parties filed cross petitions for operation and mismanagement under Sections 241 and 242 of the Companies Act, 2013 (the Act).
- After filing the main petition under Sections 241 and 242 of the Act, Rose Investments filed one more petition before NCLT for the appointment of Chief Financial Officer (hereafter called CFO) of Rattan India.
- Article 140 of the Articles of Association (AOA) of Rattan India states that Rose Investments had the right to suggest three candidates, one by one, for the post of CFO of Rattan India and if Hamlin Trust rejected the first 2 candidates suggested by Rose Investments, then they shall have to accept the appointment of the third candidate suggested by Rose Investments as CFO.
- Hamlin Trust did not accept the first 2 candidates recommended by Rose Investments and was also disputing the appointment of a third candidate. Therefore Rose Investments filed the said petition.
- NCLT, New Delhi ruled in favor of Rose Investments (petitioners before NCLT), and by passing the impugned order allowed the appointment of the third candidate suggested by Rose Investments as CFO of Rattan India.
- Aggrieved by the said order, Hamlin Trust filed an appeal before NCLAT, New Delhi

Appellants contentions

The Learned Senior Counsel for Hamlin Trust has argued that,

- As per article 140 of AOA of Rattan India, Rose Investments first suggested the name of Mr. Devendra Mehta, which was not approved by the Hamlin Trust, since he was to continue in his parent company Alvarez and Marsal India Private Limited (in short 'A&M') and would have only rendered services to the Company in accordance with his engagement agreement while continuing to work with A&M, his parent company. Further compensation for the services of CFO would have to be paid by Rattan India to A & M, and A & M will pay to Mr. Devendra Mehta.
- Thereafter, the name of Mr. Venkataraman Subramanian was suggested, which was also rejected by Hamlin Trust because he was also seconded for engagement as CFO by Deloitte Touche Tohmatsu India LLP (in short 'DTT') based on an agreement and payment for the services were to be provided to DTT considering Mr. Subramanian as an employee of DTT who would be deployed with Rattan India to work as CFO.
- Referring to sub-section 3 of Section 203, it was argued that both the candidates suggested by Rose Investments were ineligible to be appointed as CFO of Rattan India for the reason that they were already in full-time employment at other companies and Section 203(3) prohibits the appointment of 1 person as KMP in 2 companies.
- Further, it was argued that the third candidate Mr. Bipin Kabra, whose name was suggested for the post of CFO, was the Managing Director of Eunoia Financial Services Private Limited. Therefore, his nomination and the future appointment would also be in contravention of Section 203(3) of the Act. It was also pointed out that in the affidavit filed by Mr. Bipin Kabra, under the Impugned NCLT Order, Mr. Kabra has not explicitly said that he would resign from the position of Managing Director, so that may be in contravention of Section 203(3) of the Act.
- It was contended that Article 140 of AOA of Rattan India did not imply that Rose Investments had an absolute and unfettered right to nominate an ineligible and invalid candidate for appointment as CFO.
- Moreover, since Article 140 of the AOA does not stipulate any procedure or eligibility conditions for the appointment of a CFO, it is perfectly logical and rational that reference is made to the Act and rules made therein to consider the eligibility conditions for CFO.
- Also, it was submitted that the suggestion of ineligible and disqualified persons for appointment as CFO as candidate nos. 1 and 2 is a ploy by Rose Investments to ensure that its chosen candidate, who is the third suggested name, is by default appointed as CFO.

Respondent's contentions

In reply, the Learned Senior Counsel for Rose Investments has strongly argued that:

- Article 140 of AOA of Rattan India fully governs the appointment of a CFO, and the provisions of the Companies Act, 2013, particularly Section 203, are not applicable since Rattan India is a Private Limited Company.
- Article 140 of AOA does not contemplate that a person's nomination can be considered to be valid or invalid for any particular reason, and the Impugned NCLT Order accepts this argument.
- The judgment in the matter of ***Manohar Nathurao Samarth vs. Marotrao, (1979) 4 ACC 93*** was also cited to buttress the claim that the ineligibility criteria must flow from a specific provision of law. The applicability of Section 203 does not hold, and so the NCLT has correctly rejected the Hamlin Trust's contention that the nomination of first two candidates is invalid.

  It was further argued that, even if one were to accept the applicability of Section 203, Rose Investments had demonstrated that Mr Bipin Kabra fulfilled the criteria set out in Section 203(3) of the Act. Hamlin Trust cannot escape the responsibility of accepting the candidature of Mr. Bipin Kabra as the third nomination, as stipulated in Article 140 of AOA.

  It was further submitted that Mr. Kabra had filed an affidavit as required by the Impugned Order of NCLT and had bound himself to comply with the requirements of Section 189(2) and Section 203(3) of the Act regarding disclosure of interests in other entities by KMP and relinquishment of the position of KMP in other entities.

Held

The 2 issues considered by the court regarding the appointment of CFO are:

(i) Whether Article 140 of AOA is the only provision that is applicable concerning the appointment of CFO in the Company and no reference to and compliance of any provision of the Companies Act, 2013, particularly Sections 203, 184, and 189 therein, is necessary? And;

(ii) If reference to Section 203 is found to be necessary for looking at the eligibility of a suggested nomination, whether Rose Investments suggestions of the names of Mr. Devendra Mehta and Mr. Venkataraman Subramanian as first and second nominations comply with the requirement of article 140 of the AOA for appointment of CFO?

- Concerning the **first question**, the NCLAT has held that,
- The position of CFO is included as a KMP under Clause (51) of Section 2 of the Act.
- Section 6 of the Act provides that the provisions of this Act shall override anything to the contrary contained in the Memorandum or Articles of Association of a company.
- Provisions under Sections 184, 189, and 203 of the Act provide rational and reasonable norms and standards

regarding the eligibility of KMP and which are relevant and useful in conducting the affairs of the company in a transparent, independent, and unbiased manner keeping the interest of the company foremost.

- Further, the NCLAT noted that the Impugned Order of NCLT accepts the applicability of Sections 184, 189, and 203 of the Act, and it directs Mr Bipin Kabra to file an affidavit undertaking to abide by the requirements of these provisions.
- Section 203 of the Act lays down that the CFO is a Whole-Time KMP and is prohibited from holding office in more than one company except in its subsidiary company at the same time.
- Article 140 of AOA makes it clear that if JV Partner i.e., Hamlin Trust, rejects the appointment of two suggested candidates, it has to accept the nomination of the third candidate. While the right of Rose Investments' has been made primary, the text of this Article does not imply that any person, even if ineligible by the normal standard of eligibility given in Section 203 of the Act and the requirement of the CFO to be a Whole-Time KMP, can be considered a valid candidate for the position of CFO.
- In the absence of any specific mention regarding eligibility and the method of selection of the CFO in the AOA, it would be logical to take recourse to Section 203 of the Act, in the selection and appointment of CFO, and also keep in view Sections 184 and 189 in adjudging the eligibility of the KMP.
- Concerning the **second question**, the court held that,
- It was argued on behalf of Rose Investments that, Rattan India is a Private Limited Company, and Provisions of Section 203 do not apply thereto. The NCLAT's view was that the principles governing the appointment and qualification of the KMP under Section 203 could be taken for guidance de hors article 140 of the AOA. Therefore, the appellants (Hamlin Trust) are not precluded from arguing the applicability of Section 203 at the appeal stage.
- The NCLAT observed that the proposals for deployment of Mr. Devendra Mehta and Mr. Venkataraman Subramanian in Rattan India are like 'secondment'. Hence the first two suggested names, are ineligible for appointment as CFO as they contravene sub-section (3) of Section 203 of the Act.
- The import of article 140 of the AOA is certainly not that the first two suggestions could be of ineligible candidates so that the Hamlin Trust has to, then, accept the name of the third candidate as Hobson's choice.
- Therefore, NCLAT took the view that all the suggested candidates should satisfy the basic conditions of eligibility as required under Section 203 of the Act so that Hamlin Trust can exercise their right of selecting the most appropriate and suitable candidate in the true letter and spirit of the article 140 of the AOA.
- It was concluded by the NCLAT that the NCLT had committed an error in

inferring that the provision in Article 140 of the AOA does not contemplate that a person's nomination can be considered valid or invalid for any particular reason.

- NCLAT's view was that the suggested candidates should be eligible as per the provision of Section 203 of the Comp Act while applying Article 140 of the AOA.
- The Impugned Order passed by NCLT was set aside. The parties are directed to take necessary action for the appointment of the CFO of Rattan India as per Article 140 of the AOA, after making valid nominations keeping in view Section 203 of the Act and completing the appointment of CFO within a period of sixty days from the date of NCLAT Order.

IBC

In the matter of Mr. Pankaj Dhanuka, Insolvency Professional (IP) order dated 12th April 2022 passed by the Disciplinary Committee of Insolvency Bankruptcy Board of India (IBBI)

Facts of the Case

- Mr. Pankaj Dhanuka (IP) was appointed as an Interim Resolution Professional (IRP) of Corporate Power Limited, the Corporate Debtor (CD) by the National Company Law Tribunal, Kolkata (NCLT) in the matter of Asset Reconstruction Company (India) Limited vs. Corporate Power Limited vide its order dated 19th February 2020 admitting an application for Corporate Insolvency Resolution Process (CIRP) under section 7 of the Insolvency and Bankruptcy Code, 2016 (/IBC). Subsequently, Mr. Dhanuka was appointed as the Resolution Professional (RP) in the said CD.
- Insolvency Bankruptcy Board of India (IBBI) received a complaint against the IP in respect of the said CIRP, and the complaint was examined by IBBI.
- The IBBI issued the Show Cause Notice (SCN) to IP on 25th November 2021 based on the material available on record in respect of his role as an IRP and RP in the CIRP of the CD.
- The SCN alleged contravention of section 208(2)(a) and (e) of the IBC, Regulation7(2)(a) and 7(2)(h) **of the IBBI (Insolvency Professionals) Regulations, 2016 (IP Regulations) and Clause 14 and 23B of the Code of Conduct under the First Schedule of Regulation 7(2) (Code/Code of Conduct) thereof which deals with the functions and obligations of the insolvency professionals.**
- It was observed from the minutes of the 1st meeting of Committee of Creditors (CoC) that Deloitte Touche Tohmatsu India LLP (DDTIL) was appointed to provide support services to the CD. The minutes also noted that IP was an advisor of DDTIL.
- As per section- 5(24A)(g) of IBC, which deals with the related party, a limited liability partnership or partnership firm which acts on the advice of an individual is a related party in respect to that individual.
- Further, as per Clause 23B of the Code of Conduct in specified in the first schedule of IP regulations, a related

party cannot be appointed or engaged by an IP for any work related to an assignment under Code.

- Despite being an advisor of DDTIL - IP appointed DDTIL to provide support services in the CIRP of the said CD, which was in contravention of the IP Regulations. The aforesaid acts and omissions on the part of IP during the CIRP of the CD, when seen in the context of role, functions, responsibilities, and powers conferred upon an IRP/RP, suggest that the conduct was allegedly in violation of the aforementioned provisions.

Submissions made by RP

- It was submitted that he had undertaken duties and obligations during the CIRP of the CD in complete compliance with the provisions of the IBC, IP Regulations wherever applicable, as well as the Code of Conduct.
- That the said appointment was for DDTIL, providing professional advisory services to him during the CIRP.
- The DC noted from the minutes of the 1st CoC meeting stated that DDTIL was appointed by IP to provide support services in the CD. The DC noted that IP and DDTIL are related parties in as much as IP worked as an advisor of DDTIL, and despite being an advisor of DDTIL, he appointed DDTIL to provide support services in the CIRP of the said CD. That the said appointment was for DDTIL to provide professional advisory services to him during the CIRP of the said CD.
- Further, stated that as per clause 23B of the Code of Conduct, an IP should not engage/appoint any related parties in connection with any work relating to assignment under the Code. As per Section 5 (24A)(g) of the Code, in respect of an individual, a related party would consist of an LLP whose partners/employees, in the ordinary course of business, act on the advice, directions, or instructions of the individual.
- Relied on the case of Poppatlal Shah v. State of Madras wherein it was held that *"it is (a) settled rule of construction that to ascertain the legislative intent all the constituent parts of a statute are to be taken together*". *As such, the term 'advice' has to be read and interpreted in the context of the entire provision, not insolation*. Further, the Hon'ble Supreme Court in ***'Rainbow Steels & Anr. vs. Commissioner of Sales Tax, U.P. & Anr.'*** held that "*where two or more words which are susceptible of analogous meaning are coupled together, noscitur a sociis, they are understood to be used in their cognate sense. They take, as it were, their color from each other, the meaning of the more general being restricted to a sense analogous to that of the less general*."
- That the word 'advice', as used in the abovesaid provision, was restricted in its interpretation to the extent that it was analogous to the words 'directions' and ''instructions.'
- The said cardinal principle of statutory interpretation also makes it evident that "advice" as used in Section 5(24A)(g) has to be interpreted as advice

that was binding upon the partners/ employees of the LLP. Such binding nature of "advice" follows from similar connotation and import of the terms "directions" or "instructions" which immediately follow the word "advice".

- That the wording and framing of section 5(24A)(g) of IBC make it abundantly clear that it was aimed at persons on whose advice/directions/ instructions, the partnership/LLP was accustomed or required to act. The provision makes it clear that the partners/employees act on such advice, instructions, or directions in the ordinary course of business. As such, the provision cannot be said to apply to an individual who provides professional advisory services similar in his capacity as a consultant, and only provides the same as and when his/ her advice is solicited. Therefore, as used in Section 5(24A)(g) of IBC, the word "advice" cannot, by any stretch of the imagination, be said to include the advice provided by a consultant engaged by the partnership firm or LLP, as the case may be.
- Section 2(59) of the Companies Act, 2013 states that an "officer" includes any director, manager, or key managerial personnel or "any person in accordance with those directions or instructions the board of directors or any one or more of the directors is or are accustomed to act."
- It is clear that a shadow director must be a person involved very closely with the day-to-day affairs and functioning of the company and that a person who is merely a professional advisor or consultant, who provides his advice on it being solicited for a professional fee, would not be a shadow director.
- Similarly, Sec 5(24A)(g) of the Code is not attracted merely on account of an individual providing purely advisory services to an LLP, with no ability to influence the decision-making or governance of the LLP. In other words, where a professional's consultant advice is not binding on the LLP – where it may at its discretion and option may be followed or may not be followed by LLP at its discretion.
- The interpretation of section 5(24A)(g) would lead to absurd results – for instance, a lawyer appointed by the LLP, which provides legal advice to the LLP, would also, by being an advisor to the LLP, become a related party of the LLP – this could have never been the intention of the legislature.
- That in the present case, as a consultant engaged by DDTIL at its will, is, as a matter of fact, not providing any advice about the governance or management of DDTIL or any other advice to DDTIL which any of its partners or employees are required to act upon in the ordinary course.
- That DDTIL was exclusively managed and governed by its group of equity partners, who are all professionals from various fields, including but not limited to experts in the field of finance, financial advisory (including those on mergers and acquisitions), etc., and of significant standing in their own right.

- As such, IP's role with DDTIL is solely as a consultant providing certain advisory services as and when sought and is limited to one of the business lines of DDTIL, and it cannot be said to be an individual on whose advice DDTIL and its partners and/or employees are accustomed to act.
- That DDTIL is a significant organization with many employees and partners and delivers a wide array of professional services. As such, DDTIL has professional relationships with number of independent consultants, and it would be wholly incorrect to classify them as 'related parties'.
- The term 'advisor' is utilized commonly and frequently within the finance and consulting industry to denote professionals and consultants who provide a wide range of advisory and professional services.
- A professional advisory service in the CIRP of CD does not fall foul of any provisions of the IBC or Code of Conduct or of that matter of IP Regulations.

Submissions made by the Disciplinary Committee (DC) of IBBI

- Under IBC, IP/RP plays a central role in the resolution process of the CD - appointed by the NCLT as an officer of the Code of Conduct the resolution process. It was the duty of RP to conduct CIRP with integrity and accountability in the process and to take reasonable care and diligence while performing the duties. Therefore, it becomes imperative for an IP to perform duties with utmost care and diligence.
- RP was expected to function with reasonable care and diligence to ensure the credibility of the process.
- From the minutes of the 1st CoC meeting that DDTIL was appointed by IP to provide support services in the CD. The DC also noted that IP and DDTIL are related parties in as much as IP worked as an advisor of DDTIL, and despite being an advisor of DDTIL, IP appointed DDTIL to provide support services in the CIRP of the said CD.
- In the instant matter, the submission of IP that restricted interpretation is to be given with respect to the advice given during the engagement as a consultant to DDTIL is not tenable. When a firm engages a professional, usually, the advice given by the individual is acted upon as it is from a professional person, and it gives authenticity to the advice. For that purpose, a consultation fee is also paid. Thus, the DC finds that IP has contravened the provisions of the IBC and the Code of Conduct by engaging DDTIL as its support service provider.

Held

- The DC held that IP should not undertake any assignments under the Code for a period of one year from the date of coming into force of the above order.

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