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DUE DILIGENCE AND CORPORATE COMPLIANCE MANAGEMENT
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QUESTION PAPER OF PREVIOUS SESSION
LEARNING OBJECTIVES

The objective of this study lesson is to enable the students to understand

- Meaning, nature, objectives, significance, scope of due diligence, need for due diligence
- Types of Due diligence
- Steps involved in due diligence
- Various transactions requiring due diligence exercise

I. INTRODUCTION

It is the process by which confidential legal, financial and other material information is exchanged, reviewed and appraised by the parties to a business transaction, which is done prior to the transaction.

“Due diligence” is an analysis and risk assessment of an impending business transaction. It is the careful and methodological investigation of a business or persons, or the performance of an act with a certain standard of care to ensure that information is accurate, and to uncover information that may affect the outcome of the transaction.

It is basically a “background check” to make sure that the parties to the transaction have the required information they need, to proceed with the transaction.

Due diligence is used to investigate and evaluate a business opportunity. The term due diligence describes a general duty to exercise care in any transaction. As such, it spans investigation into all relevant aspects of the past, present, and predictable future of the business of a target company.

Due diligence report should provide information and insight on aspects such as the risks of a transaction, the value at which a transaction should be undertaken, the warranties and indemnities that needs be obtained from the vendor etc.

II. NATURE OF DUE DILIGENCE IN DIFFERENT CONTEXTS

The nature of due diligence varies from the type of transaction, its volume, the motive and objective of parties to a transaction. The nature and the extent of due diligence depends upon the risk perceived by parties to a transaction. The nature of due diligence may be explained under the following heads.

(i) Business and Commercial Transactions
In business transactions, the due diligence process varies for different types of companies nature and volume of transactions etc. The relevant areas of concern may include the financial, legal, labour, tax, environment and market/commercial situation of the company. Other areas include intellectual property, real and personal property, insurance and liability coverage, debt instrument review, employee benefits and labour matters, immigration, and international transactions.

(ii) Civil Litigation

In civil litigation, due diligence is an effort made by an ordinarily prudent or reasonable party to avoid harm to another party. Failure to make this effort may be considered negligence. This is conceptually distinct from investigative due diligence, involving a general obligation to meet a standard of behaviour. Quite often a contract will specify that a party is required to provide due diligence.

(iii) Information Security aspects

Information security due diligence is often undertaken during the information technology procurement process to identify risks involved in protecting and maintaining information and to take remedial actions.

(iv) Money Laundering

Compliance with provisions of prevention of Money Laundering Act, 2002, guidelines issued by SEBI and RBI on know your customers (KYC) etc. will get covered under this head.

(v) Technology transfer

Aspects relating to intellectual property rights, patents, copyright, design, trademark, brand etc., are to be analysed from legal and financial angle.

III. NEED FOR DUE DILIGENCE AND ITS ‘SIGNIFICANCE’

Misrepresentations and fraudulent dealings are not always obvious or straight. These are to be uncovered, especially in a major business transaction, as it would create a major impact on the business. Proper due diligence services explore and assess the details behind the same and to become fully informed about the financials, business, internal systems, profitability, key operational aspects, management team, promoters and other material factors that will help in making an informed decision about an investment. Due diligence is designed to protect the interests of the Company by providing objective and reliable information on the target company before making any written commitments.

Due diligence is an investigative process for providing, the desired comfort level about the potential investment and to minimize the risks such as hidden uncovered liabilities, poor growth prospects, price claimed for proposed investment being on higher side etc. Due diligence is also necessary to ensure that there are no onerous contracts or other agreements that could affect the acquirer's return on investment.

The procedures and analyses ultimately represent a window into the target Company’s success and potential, including what opportunities exist to grow the business further to meet your goals and objectives. Due diligence exercise is needed
to confirm that the nature and genuineness of a business, Identify defects/weakness in the target company and to avoid a bad business transaction, to gather information that is required for valuation of assets, and to negotiate in a better manner. In nutshell due diligence is a SWOT analysis of an investment which is essentially required to make an informed decision about a potential investment.

Due diligence is necessary to allow the investigating party to find out everything that one needs to know about the subject of the diligence. The objective is to allow the investigator to consider the following options, considering the facts found in the course of due diligence.

(i) **Withdrawal of deal** – if the due diligence uncovers information that disclosed the investments, loan or participation, a risky or undesirable one and which cannot be adequately resolved then the investigator may withdraw from the deal.

(ii) **Adjusting the valuation of the investment** – the investigator may revise his valuation of the company or reassess the price at which it will provide services. More often, the information will be adverse and therefore the valuation will go down or the price will go up.

(iii) **Solving of problems uncovered** – it may be possible for a problem uncovered by the due diligence to be solved before the deal goes ahead. For example, unpaid stamp duty could be paid, company filings could be put in order or, if negative information is uncovered on a principal of the target company, the investor may put pressure on the target is put into a state that the investigator is happier with before it deals with it.

IV. OBJECTIVES OF DUE DILIGENCE

The objective of due diligence is to verify the strategic identification or attractiveness of the target company, valuation, risk associated etc.

The objective of due diligence may be to—

1. Collect material of information from the target company.
2. Conduct a SWOT analysis to identify the strength and to uncover threats and weaknesses.
3. For improving the bargaining position depending on SWOT analysis.
4. To take an informed decision about an investment.
5. Identification of areas where representations and warranties are required.
6. To provide a desired comfort level in a transaction.
7. To ensure complete and accurate disclosure.
8. Bridge the gap between the existing and expected.
9. To take smooth/accurate action/decision.
10. To enhance the confidence of stake holders.

The SWOT analysis of the target business carried out as a part of due diligence has to reveal the strengths and weaknesses of not only the financials but also intangibles. To do this effectively, the potential buyer needs to be clear about the
goals and motives for acquiring the target company, as well as the value the buyer is attempting to create with the purchase. For example, if there is a legal risk, such as an outstanding lawsuit, that will not only jeopardize the financial stability of the company but also the loyalty of existing customers. This will erode the target company’s market of customers by a new and stronger competitor. The target company’s talent is the asset desired, and much of this depends on employee relations and accordingly cultural issues has to be addressed in time.

A thorough due diligence helps to reveal any of the negatives, but the process of due diligence rarely goes smoothly because of one major stumbling block and that is availability of information. The target company is rarely eager to reveal to the other party that it is up for sale and wants to keep this information confidential from its competitors, customers and employees. So getting any information from these sources can be tricky, depending upon what the potential buyer wants to gain from the transaction. The buyer who aims to get new market of customers with the transaction wants to make sure that the target company has a good relationship with existing customers. But, during due diligence, the target company does not want any contact with its existing customers for fear that customers might leave because of the impending sale. As another example, a potential buyer sees the employee talent as the company’s main asset, but the target company is nervous about letting the potential buyer talk to key employees because it does not want to let on that it is going to be sold. Because of the confidential nature of transactions, not all the information that is necessary to make a good decision can be revealed. This is why services of experts are hired in due diligence before beginning the process so the buyer receives reliable guidance. It is also critical to meet with trusted advisors—both inside and outside about what has been discovered and brainstorm the different scenarios of what can go wrong before going ahead with the deal.

Once a purchase price is agreed upon the prospective buyer usually enters into a conditional agreement with a due diligence clause with the target business, in which the buyer has a limited period to conduct due diligence. During this time, the potential buyer requests full access to all relevant materials in the target business, all customer, vendor, financial and other information in order to conduct a thorough investigation. Here it is to be ensured that the potential buyer does not use this information for its own benefit if it decides to back out of the deal, a confidentiality agreement is usually signed to protect the target businesses’ interests. But a possibility of re-negotiation of the purchase price or cancellation of the agreement on the part of buyer is seen if the information found is not acceptable to the potential buyer. Again after due diligence, the goal is to either reaffirm the purchase price or renegotiate, depending on what was discovered. But the ultimate goal is to make a rational decision based on the facts. While it may be hard to overcome the excitement of purchasing a business, here the potential buyer is prepared to cancel the deal as earlier said if something is discovered that runs counter to why the business looked like a good deal in the first place.

V. SCOPE OF DUE DILIGENCE

Scope of due diligence is transaction-based and is depending on the needs of the people who is involved in the potential investments, in addressing key uncovered issues, areas of concern/threat and in identifying additional opportunities.
Due diligence is generally understood by the legal, financial and business communities/potential investors to mean the disclosure and assimilation of public and proprietary information related to the assets and liabilities of the business being acquired. This information includes financial, human resources, tax, environmental, legal matters, intellectual property matters etc.

Due diligence would include thorough understanding of all the obligations of the target company: debts, rights and obligations, pending and potential lawsuits, leases, warranties, all high and impact laden contracts – both inter-corporate and intra-corporate.

The investigation or inspection would cover:
- Compliance with applicable laws
- Regulatory violations or disciplinary actions
- Litigation and assessment of feasibility of pursuing litigation
- Financial statements
- Assets – real and intellectual property, brand value etc.
- Unpaid tax liens and/or judgements
- Past business failures and consequential debt
- Exaggerated credentials/Fraudulent claims
- Misrepresentations or character issues
- Cross-border issues – double taxation, foreign exchange fluctuation, sovereign risk, investment climate, cultural aspects.
- Reputation, goodwill and other intangible assets.

VI. TYPES OF DUE DILIGENCE

In business transactions, the due diligence process varies for different types of companies. The relevant areas of concern may include the financial, legal, labour, tax, environment and market/commercial situation of the company. Other areas include intellectual property, real and personal property, insurance and liability coverage, debt instrument review, employee benefits and labour matters, immigration, and international transactions. The most important types of Due Diligence are:

A. Business Due Diligence
   (i) Operational due diligence
   (ii) Strategic due diligence
   (iii) Technical due diligence
   (iv) Environmental due diligence
   (v) Human Resource Due diligence
   (vi) Information Security due diligence

B. Legal Due Diligence (including secretarial due diligence)
C. Financial Due Diligence (including tax due diligence).

A. Business Due Diligence

Business due diligence involves looking at quality of parties to a transaction, business prospects and quality of investment. It involves,

(i) Operational due diligence

Operational due diligence aims at the assessment of the functional operations of the target company, connectivity between operations, technological upgradation in operational process, financial impact on operational efficiency etc. It also uncovers aspects on operational weakness, inadequacy of control mechanisms etc.

(ii) Strategic due diligence

Strategic due diligence tests the strategic rationale behind a proposed transaction and analyses whether the deal is commercially viable, whether the targeted value would be realized. It considers factors such as value creation opportunities, competitive position, critical capabilities.

(iii) Technical Due Diligence

Technical due diligence covers—
(a) intellectual property due diligence; and
(b) technology due diligence.

(a) Intellectual Property due diligence

The recent concept of valuation of intangible assets related to Intellectual Property like Patents, Copyrights, Design, Trademarks, Brands etc., also getting greater importance as these Intellectual Properties of the business are now often sold and purchased in the market by itself, like any other tangible asset. Many Indian companies and corporate entities however do not give much importance to the portfolio management of their Intellectual Property Rights (IPR). The main objective of intellectual property due diligence is to ascertain the nature and scope of target company’s right over the intellectual property, to evaluate the validity of the same and to ensure whether there is no infringement claims.

(b) Technology due diligence

Technology due diligence considers aspects such as current level of technology, company’s existing technology, further investments required etc. Technology is a key component of merger and acquisition activities; it’s imperative to look at IT considerations.

(iv) Environmental Due Diligence

Environmental due diligence analyses environmental risks and liabilities associated with an organisation. This investigation is usually undertaken before a merger, acquisition, management buy-out, corporate restructure etc.

Environmental due diligence provides the acquirer with a detailed assessment of the historic, current and potential future environmental risks associated with the target
organisations sites and operations.

It involves risk identification and assessment with respect to:

(a) review the environmental setting and history of the site
(b) assessment of the site conditions
(c) operations and management of sites
(d) confirm legal compliance and pollution checks from regulatory authorities etc.

(v) Human Resource Due Diligence

Human Resource Due Diligence aims at people or related issues. Key managers and scarce talent leave unexpectedly. Valuable operating synergies gets disturbed, when cultural differences between companies aren’t understood or are simply ignored. It’s crucial to consider cultural and employees issues upfront, for success of any venture.

(vi) Information Security Due Diligence

Information security due diligence is often undertaken during the information technology procurement process to ensure that risks are uncovered.

(vii) Ethical Due Diligence

Ethical Due Diligence measures ethical character of the company and identify the possibilities of ethical risks, which is a non-financial risk. It may relate to reputation, governance, ethical values etc. It helps an organization to decide whether the partner is ethically viable. This is an effective reputation management tool for any type of business decisions.

B. Legal Due Diligence

A legal due diligence covers the legal aspects of a business transaction, liabilities of the target company, potential legal pitfalls and other related issues. Legal due diligence covers intra-corporate and intercorporate transactions.

It includes preparation of regulatory checklists meeting with personnel, independent check with regulatory authorities etc. apart from document verification.

C. Financial Due Diligence

Financial due diligence provides peace of mind to both corporate and financial buyers, by analysing and validating all the financial, commercial, operational and strategic assumptions being made.

Financial Due Diligence includes review of accounting policies, review of internal audit procedures, quality and sustainability of earnings and cash flow, condition and value of assets, potential liabilities, tax implications of deal structures, examination of information systems to establish the reliability of financial information, internal control systems etc.
The tax due diligence comprises an analysis of:

- tax compliance
- tax contingencies and aggressive positions
- transfer pricing
- identification of risk areas
- tax planning and opportunities

VII. FACTORS TO BE KEPT IN MIND WHEN CONDUCTING DUE DILIGENCE

Objectives and purpose

A key step in any due diligence exercise is to develop an understanding of the purpose for the transaction. The goal of due diligence is to provide the party proposing the transaction with sufficient information to make a reasoned decision as to whether or not to complete the transaction as proposed. It should provide a basis for determining or validating the appropriate terms and price for the transaction incorporating consideration of the risks inherent in the proposed transaction. The following factors may be kept in mind in this regard:

(i) Be clear about your expectations in terms of revenues, profits and the probability of the target company to provide you the same.

(ii) Consider whether you have resources to make the business succeed and whether you are willing to put in all the hard work, which is required for any new venture.

(iii) Consider whether the business gives you the opportunity to put your skills and experience to good use.

(iv) Learn as much as you can about the industry you are interested in from media reports, journals and people in the industry.

Planning the schedule

Once it is decided for a particular business, make sure of the following things:

- Steps to be followed in due diligence process
- Areas to be checked
- Aspects to be checked in each area
- Information and other material to be requested from the seller

Negotiation for time

Some times, it may be the case that, sellers want the process to get over as soon as possible and try to hurry the proceedings. When the seller gives a short review period, negotiations can be made for adequate time to have a complete review on crucial financial and legal aspects.

Risk Minimisation

All the information should be double checked—financials, tax returns, patents,
copyrights and customer base to ensure that the company does not face a lawsuit or criminal investigation. The financials are very important and one needs to be certain that the target company did not engage in creative accounting. The asset position and profitability of the company are vital.

Since, Due diligence exercise deals with the overall business, it is important to consider aspects such as:
- background of promoters
- performance of senior management team
- organizational strategy
- business plans
- risk management system
- technological advancement
- infrastructure adequacy
- optimum utilization of available resources

**Information from external sources**

The company’s customers and vendors can be quite informative. It may be found from them whether the target company falls in their most favored clients list.

Any flaws that the audit uncovers would help to negotiate down the sale price. Due diligence is “a chance to get a better deal”. But don’t go overboard. Remember that the whole point of buying a company is to add people to your own organization. Even if the seller and staff do not stay on after the deal, they may prove useful as advisers in the future.

**Limit the report with only material facts**

While preparing the report it is advisable to be precise and only the information that has a material impact on the target company is required to be included.

**Structure of information**

Once the due diligence process is over, while preparing the report, information has to be structured in an organized manner in order to have a better correlation on related matters.

**VIII. STAGES/PROCESS OF DUE DILIGENCE**

A due diligence process can be divided into three stages (i) pre diligence, (ii) diligence, and (iii) post diligence.

**(i) Pre diligence**

A pre diligence is primarily the activity of management of paper, files and people.

1. Signing the Letter of Intent (LOI) and the Non Disclosure Agreement (NDA)/ Engagement letter.
2. Receipt of documents from the company and review of the same with the checklist of documents already supplied to the company.
3. Identifying the issues.
4. Organising the papers required for a diligence.
5. Creating a data room.

The first and foremost in a deal for the management of the target company, is that the investor is to sign a Letter of Intent (LOI) or a term sheet which underlines the various terms on which the proposed deal is to be concluded. Immediately on receipt of the LOI the investors sign an NDA with the various agencies conducting a diligence, be it finance, accounting, legal or a secretarial diligence.

The company, would usually receive a checklist from the agency conducting the diligence. The checklist is invariably exhaustive in nature, and therefore, the company may either collate and compile the documents in-house, or outsource this to an external agency. While the data is being collated care should be taken to ensure that there are no loose ends that may probably arise.

As regards a data room, some of the important things that one should take cognizance of from the corporate view point are the following:

(a) Do not delay deadlines (leads to suspicion).
(b) Mark each module of the checklist provided for separately.
(c) In case some issues are not applicable spell it out as "Not Applicable".
(d) In case some issues can not be resolved immediately, admit it.
(e) Put a single point contact to oversee the process of diligence.
(f) Keep a register, to track people coming in and going out.
(g) An overview on the placement of files.
(h) Introduction to the point person.

During the diligence, care should be taken to adhere to certain hospitality issues, like:

(a) Be warm and receptive to the professionals who are conducting diligence.
(b) Enquire on the DD team.
(c) Join them for lunch.
(d) Ensure good supply of refreshments.
(e) In case of any corrections – admit and rectify.

As regards the process of diligence, as a professional care should be taken to scrutinize every document that is made available and ask for details and clarifications, though, generally the time provided to conduct the diligence may not be too long and though things have to be wrapped up at the earliest. The company may be provided an opportunity to clear the various issues that may arise out of the diligence.

(ii) Diligence

After the diligence, is conducted, the professionals submit a report, which is
common parlance is called the DD report. These reports can be of various kinds, a summary report; a detailed report or the like; and the findings mentioned in the report can be very significant, in as much as the deal is concerned.

There are certain terms used to define the outcome of these reports:

**Deal Breakers:** In this report the findings can be very glaring and may expose various non-compliance that may arise – any criminal proceedings or known liabilities.

**Deal Diluters:** The findings arising out a diligence may contain violations which may have an impact in the form of quantifiable penalties and in turn may result in diminishing the value of company.

**Deal Cautioners:** It covers those findings in a diligence which may not impact the financials, but there exist certain non compliances which though rectifiable, require the investor to tread a cautious path.

**Deal Makers:** Which are very hard to come by and may not be a reality in the strict sense, are those reports wherein the diligence team have not been able to come across any violations, leading them to submit what is called a ‘clean report’.

Interestingly, only after the reporting formalities are over and various rectifications are carried out, the "shareholders agreement" (which is the most important document) is executed. This agreement contains certain standard clauses like the tag along and drag along rights; representations and warranties; condition precedents, and other clauses that have an impact on the deal.

(iii) Post Diligence

Post diligence sometimes result in rectification of non-compliances found during the course of due diligence. There can be interesting assignments arising out of the diligence made by the team of professionals. It can range from making applications/filing of petition for compounding of various offences or negotiating the shareholders’ agreement, since the investors will be on a strong wicket and may negotiate the price very hard.

**IX. TRANSACTIONS REQUIRING DUE DILIGENCE**

1. **Mergers, amalgamations and Acquisitions**

Due diligence investigations are generally for corporate acquisitions and mergers– i.e., investigation of the company being acquired or merged. These are also generally the most thorough types of due diligence investigations. The buyer or transfree company wants to make sure it knows what it is buying. Partnerships are another time when parties investigate each other in conjunction with negotiations. Some other transactions where due diligence is appropriate could be:

(a) Strategic Alliances, and Joint Ventures

(b) Strategic partnerships

(c) Partnering Agreements
As regards the acquirer due diligence is an opportunity to confirm the correct value of the business transaction, accuracy of the information disclosed by the target company as well as determines whether there are any potential business concerns that need to be addressed. This process helps evaluation and plan for the integration of business between the transacting parties. As regards the target company, it is ascertaining the ability of the acquirer to pay or raise funds to complete the transaction, of rights that should be retained by the target company, determination of any obstacles that could delay the closing and aid in the preparation of the target company's disclosure schedules for the definitive and final transactional document.

2. Joint venture and collaborations

Before entering into a major commercial agreement like a joint venture or other collaboration with a company, a collaboration partner will want to carry out a certain amount of due diligence. This is particularly likely to be the case where a large company is forming a relationship for the first time with a relatively small start-up company. The due diligence may not to be as extensive as in an acquisition, but the larger company will be seeking comfort that its investment will be secure and the small company has the systems personnel, expertise and resources to perform its obligations.

3. Venture Capital Investment

Before making an investment in any company, venture capitalizes will conduct business due diligence, which generally includes aspects such as a review of the market for the product of the company, background check on the founders and key management team, competition for the company, discussions with key customers of the company, analysis of financial projections for the business, review of any weakness/differences in the management team, minutes and consents of the board of directors and shareholders, corporate charter and bylaws, documents on litigations, patents and copyrights, and other intellectual property-related documents etc.

4. Public Offer

Public issue due diligence spans the entire public issue process. The steps involved may be

1. Decisions on public issue.
2. Business due diligence.
3. Legal and financial due diligence.
4. Disclosures in prospectus.
5. Marketing to investors.
6. Post issue compliance.
Under the SEBI (Disclosure & Investor Protection) Guidelines, 2000 Merchant Bankers are required to issue a due diligence certificate and they conduct an extensive due diligence process on the company.

X. DOCUMENTS TO BE CHECKED IN DUE DILIGENCE PROCESS

The following are the few types of information or documents to be checked, during the process of due diligence.

1. Basic information
2. Financial Data
3. Important business Agreements
4. Litigation aspects
5. IPR Details
6. Marketing information
7. Internal control system
8. Taxation aspects
9. Insurance coverage
10. Human resources aspects
11. Environmental impact
12. Cultural aspects

However, the list mentioned above is not an exhaustive. The purpose of providing this list is to provide a general idea of documents that are required to be checked in any type of due diligence.

XI. THE CONCEPT OF DATA ROOM IN DUE DILIGENCE

What is data room?

A Data Room provides all important business documents/information which may be on Financial, regulatory, IPR, marketing, Press report or any important material aspect pertaining to a business transaction. Other wise it provides for a common platform/place where all records of important business information are kept for the review by a potential buyer after signing of a Non Disclosure Agreement (NDA). As data room discloses confidential data which is not available for public and may relate to business process, trade secret, technology information etc, the access to data room is made after signing of Non Disclosure Agreement.

Provisions are also made to mitigate the risks of data destruction or data stealing. For this purpose the restrictive provisions are made for entry, study, noting and exit from the data room. This includes physical checking of the persons conducting such study in the data room. Installing close circuit camera in the data room and monitoring the activity of the persons on time to time basis is a regular activity. It results in adequate expenditure and prior to that make proper budgeting is required.

Principals are also laid down for copying documents to clearly state about the nature of documents which could be copied in the data room. For this purpose also
photocopiers and scanning machines are kept, electronic data similarly also monitored for which copies are required to be made.

**Why Data Room?**

1. Removes ambiguity in the minds of buyer about the profitability, growth prospectus, and sustainability of business that is proposed to be bought.
2. Provides material information that helps in doing a SWOT analysis.
3. It enables the buyer to do a better bargain through the analysis of the data.
4. May expose the weakness of the seller which is not directly provided to the buyer- For example, a material off balance sheet transaction.
5. Provides data that helps in better Valuation of business for both buyer and seller.

**What type of information is provided under a data room?**

The following are the examples of information that is provided in a Data Room. This list is not however exhaustive.

1. Financial documents such as Annual Reports, Financial statements filed with regulatory authorities, cash flow statements, documentation with bankers etc.
2. Basic corporate documents such as certificate of incorporation, Memorandum and Articles of Association, Share-holding agreement, various types of registrations, documents on General and Board Meetings, insurance contracts etc.
3. HR information
4. Equipment and information on operational aspects.
5. Information relating to sales, marketing etc
6. Compliance related information
8. IPR details
9. Information on litigation

**Some Occasions those require creation of Data Room.**

1. Mergers, amalgamations and Acquisitions
2. Strategic Alliances
3. Partnering agreement
4. Business Coalitions
5. Outsourcing agreement
6. Technology or Product Licensing
7. Joint Ventures through technical or financial collaboration
8. Venture Capital investment
9. Public Issue
Data Room – Virtual or Physical

Earlier data room was a physical location where all confidential and other documents are kept in a paper form and were kept under lock and key with custody of a responsible person. Generally the data room was created at vendor’s premises or lawyer’s office and specific time was allotted to the buyer and the authorised representatives of the buyer to enter and exit the premises which were set up as Data Room. Only one prospective buyer was allowed to view the documents at a time. When a prospective bidder demands additional or new documents it was provided to them in physical copy through courier or registered post. It demanded the physical availability of experts from different fields at the place where the due diligence exercise was being carried out.

Under the prevailing globalised economy, using of traditional physical data rooms for due diligence is not only a time-consuming and difficult process but also is very expensive as it demands the prospective buyers to travel from their place to the place where the data room is located.

Technology has enhanced the efficiency of many business processes and activities. New and creative uses of technology are expected to have similar positive effects on existing businesses. Introduction of Virtual Data Room which is an effect of technology has come as a boon for due diligence exercise.

Virtual Data Room is a site where all the required data of the prospective buyer are stored in digitalized or electronic form. Due diligence exercise these days is carried out through creation of virtual data room in the form of internet site where all the confidential/material business information is stored.

In general the following steps are involved in creation of a virtual data room.

1. Demands of the prospective bidders are identified.
2. Identify a trust worthy data room service provider if necessary and enter into necessary agreement with them.
3. Creation of a website where all the required documents are stored with internet security, restriction to access the site etc.
5. Service agreement with data room service provider and the prospective bidder.
6. Prospective bidders, on signing of Non-Disclosure Agreement and the service agreement, are given Use Id and pass word of the virtual data room so that any number of prospective bidders and access to it.

Major Advantages of Virtual Data Room

1. Savings in cost
2. Saving in time
3. More Comfort to buyer and Seller
4. Availability of information at any time of the day
5. Enables multiple prospective bidders to access the Virtual Data Room
6. Easy to Set up  
7. More Secured  
8. Improved Efficiency  
9. Copying/printing of documents may be restricted.  
10. Closure of Virtual Data Room may happen at any time  

**Some Disadvantages of Virtual Data Room**  
1. Limited interaction with prospective sellers.  
2. Lack of clarity of documents loaded on the data-site  
3. Inability to copy or print information some times becomes a hurdle  
4. Access to sensitive information such as contracts to third parties poses legal challenges relating to confidentiality of information.  

**Virtual and Physical Data Room – A comparison**

<table>
<thead>
<tr>
<th>Sl No.</th>
<th>Particulars</th>
<th>Physical Data Room</th>
<th>Virtual Data Room</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Form of documents</td>
<td>Papers, files, boxes or any tangible thing</td>
<td>Electronic/Digital/soft copies of documents including video/audio documents</td>
</tr>
<tr>
<td>2</td>
<td>Security of documents</td>
<td>Lies with the integrity of person who is in charge of the data room</td>
<td>More secured through specific log-in id and pass word. In addition facilities like internet firewalls are there.</td>
</tr>
<tr>
<td>3</td>
<td>Time required for creation of data room</td>
<td>Longer time required.</td>
<td>Can be created within 48 hours also once demands of prospective bidders are identified.</td>
</tr>
</tbody>
</table>
| 4      | Cost                                     | High because of reasons like—  
Requirement of one person to take care of data room.  
Requires bidders to travel from their place to the place of location of data room etc | Low as the documents can be viewed from any location with internet security.       |
<p>| 5      | Convenience                              | Low Level because of                                                             | More convenient as it                                                             |</p>
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<tr>
<td>6</td>
<td>Accessibility to data room</td>
<td>Restricted time</td>
</tr>
<tr>
<td>7</td>
<td>Facility to restrict access of document access</td>
<td>Not there</td>
</tr>
<tr>
<td>8</td>
<td>Facility to check who has reviewed what documents and how many times</td>
<td>Not available</td>
</tr>
<tr>
<td>9</td>
<td>Facility to highlight new information</td>
<td>To be conveyed manually to all bidders</td>
</tr>
<tr>
<td>10</td>
<td>Ability to copy documents</td>
<td>Possible</td>
</tr>
<tr>
<td>11</td>
<td>One to one communication in person with the seller or his representatives</td>
<td>Available</td>
</tr>
</tbody>
</table>

**Data room administration and data security**

Administration of data room and its management including entry access and other security aspects including data security to be planned in detail and a trial run to be conducted before making the data room operational.

**XII. DUE DILIGENCE Vs AUDIT**

An audit is concerned with historical financial statements only and provides an opinion as to whether the financial statements represent a “true and fair” view of the company's operations. Due diligence, on the other hand, review not only look the historical financial performance of a business but also consider the forecast financial performance for the company under the current business plan. The following table describes the difference between Due Diligence and Audit.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Audit</th>
<th>Due diligence</th>
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<tbody>
<tr>
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</tr>
<tr>
<td>Scope</td>
<td>Limited to financial analysis</td>
<td>Includes not only analysis of financial statements, but also business plan, sustainability of business, future aspects, corporate and management structure, legal issues etc.</td>
</tr>
<tr>
<td>-----------</td>
<td>-------------------------------</td>
<td>---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>Data</td>
<td>Based on historical data</td>
<td>Covers future growth prospects in addition to historical data.</td>
</tr>
<tr>
<td>Mandatory</td>
<td>Mandatory</td>
<td>Mandatory based on the transaction.</td>
</tr>
<tr>
<td>Assurance</td>
<td>Positive assurance i.e. true and fairness of the financial statements</td>
<td>Negative assurance. i.e. identification of risks if any.</td>
</tr>
<tr>
<td>Type</td>
<td>Post mortem analysis</td>
<td>It is required for future decision.</td>
</tr>
<tr>
<td>Nature</td>
<td>Always uniform</td>
<td>Varies according to the nature of transaction</td>
</tr>
<tr>
<td>Repetitiveness</td>
<td>Recurring event</td>
<td>Occasional event</td>
</tr>
</tbody>
</table>

**XIII. CONCLUSION**

The due diligence review should provide an overall evaluation of the viability of the target business. The due diligence reports will form a valuable tool for the new owners of the business in providing an overview of the business and identification of areas of weaknesses and threats which will have to be addressed.

Each due diligence review is unique but the overall aim is to provide the investor with sufficient, relevant and timely information in order to assist in the investment decision. The due diligence exercise is not simply a number crunching exercise but involves collation of strategic non financial information which is likely to be crucial in the overall investment decision.

The successful performance of a due diligence investigation is dependent upon the scope, planning, co-ordination and the use of a highly skilled team.

The cost of the preparation of a quality due diligence exercise is insignificant when compared to the cost of a bad acquisition.
LESSON ROUND-UP

- Due diligence is an analysis and risk assessment of an impending commercial transaction.
- Due diligence report should provide information and insight on aspects such as the risks of a transaction, the value at which a transaction should be undertaken, the warranties and indemnities that needs be obtained from the vendor etc.
- Due diligence would include full understanding of all the obligations of the target company: debts, rights and obligations, pending and potential lawsuits, leases, warranties, all high and impact laden contracts – both inter-corporate and intra-corporate.
- The stages in due-diligence may be pre-diligence, diligence and post diligence.
- Types of Due diligence may be business due diligence, legal due diligence and financial due diligence etc.
- Transaction requiring Due Diligence exercise generally includes acquisitions and mergers, Joint-venture agreements, Partnership agreements, venture capital investments etc.

SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation)

1. Briefly discuss the meaning and importance of due diligence?
2. Explain various types of due diligence?
3. Explain the stages of due diligence?
4. What are the various types of transactions that requires due diligence exercise?
5. What are the factors to be kept in mind while conducting due diligence exercise?
6. Explain the concept of data room relating to due diligence.
LEARNING OBJECTIVES
The objective of this study lesson is to enable the students to understand
• Various types of issues
• SEBI (DIP) Guidelines, 2000
• Securities and Exchange Board of India (Employee Stock Option Scheme and
  Employee Stock Purchase Scheme) Guidelines, 1999
• Pre & Post issue due diligence of IPO/FPO, Rights, Bonus, ESOP and
  Preferential issues.

I. INTRODUCTION AND REGULATORY FRAMEWORK

Introduction*
Primarily, issues can be classified as a Public, Rights or preferential issues (also
known as private placements). While public and rights issues involve a detailed
procedure, private placements or preferential issues are relatively simpler. The
classification of issues is illustrated below:

![Issues Diagram]

1 This chapter is as per the supplement issued along with the study material.
* Source: sebi.gov.in
Fresh Issue Offer for sale Fresh Issue Offer for sale

Initial Public Offering (IPO) is when an unlisted company makes either a fresh issue of securities or an offer for sale of its existing securities or both for the first time to the public. This paves way for listing and trading of the issuer’s securities.

A further public offering (FPO) is when an already listed company makes either a fresh issue of securities to the public or for sale to the public, through an offer document. An offer for sale in such a scenario is allowed only if it is made to satisfy listing or continuous listing obligations.

Rights Issue (RI) is when a listed company which proposes to issue fresh securities to its existing shareholders as on a record date. The rights are normally offered in a particular ratio to the number of securities held prior to the issue. This route is best suited for companies who would like to raise capital without diluting stake of its existing shareholders unless they do not intend to subscribe to their entitlements.

Bonus issue: When an issuer makes an issue of securities to its existing shareholders as on a record date, without any consideration from them, it is called a bonus issue. The shares are issued out of the Company’s free reserve or share premium account in a particular ratio to the number of securities held on a record date.

A private placement is an issue of shares or of convertible securities by a company to a select group of persons under Section 81 of the Companies Act, 1956 which is neither a rights issue nor a public issue. This is a faster way for a company to raise equity capital. A private placement of shares or of convertible securities by a listed company is generally known by name of preferential allotment. A listed company going for preferential allotment has to comply with the requirements contained in Chapter VII of SEBI (Issue of Capital and Disclosure Requirements) Regulations 2009.

“qualified institutions placement” means allotment of eligible securities by a listed issuer to qualified institutional buyers on private placement basis in terms of SEBI (Issue of Capital and Disclosure Requirements) Regulations 2009.

Regulatory Framework
Public issue is mainly governed by the following legislations/regulations/rules:
1. The Companies Act, 1956
2. Securities Contracts (Regulation) Act, 1956
3. Foreign Exchange Management Act, 1999
4. Securities Contracts Regulation (Rules) 1957
5. SEBI (ICDR) Regulations 2009
6. Listing Agreement

II. DUE DILIGENCE-IPO/FPO
When the due diligence is carried out as part of the steps leading to an IPO, the exercise takes on added meaning and encompasses a wider scope, as it identifies the areas or the issues where the company exhibits weaknesses and the due diligence process becomes a tool, which shows the company the way to optimize its potential and thereby increasing its value to potential investors. Pre-IPO due diligence process will result in a gap analysis between the present status of the company and the company that should be floated i.e., a gap is an expectations gap created as a result of how the market expects a listed company to conduct its affairs. In this scenario, once these gaps have been highlighted the due diligence exercise
should not stop there but should include advice given by the advisors to the company on the processes and activities which are required to fill the gaps identified. In an IPO the due diligence exercise is a broader, fuller exercise which apart from identifying the weaknesses also looks at resolving them with the purpose of increasing the value of the company.

The due diligence process aspires to achieve the following:
— to assess the reasonableness of historical and projected earnings and cash flows;
— to identify key vulnerabilities, risk and opportunities;
— to gain an intimate understanding of the company and the market in which the company operates such that the company’s management can anticipate and manage change;
— to set in motion the planning for the post-IPO operations.

It will result in a critical analysis of the control, accounting and reporting systems of the company and a critical appraisal of key personnel. It will identify the value drivers of the company thus enabling the directors to understand where the value is and to focus their efforts on increasing that value.

Due diligence spans the entire public issue process. The steps involved in due diligence are given broadly below:
1. Decision on public issue
2. Business due diligence
3. Legal and Financial Due Diligence
4. Disclosures in Prospectus
5. Marketing to Investors
6. Post issue compliance

Key areas to be focused:
(a) the financial statements – to ensure their accuracy;
(b) the assets – confirm their value, condition existence and legal title;
(c) the employees – identification and evaluation of the key movers and shakers;
(d) the sales strategy – analyzing the policies and procedures in place and assessing what works and what does not;
(e) the marketing – what is driving the business and is it effective?
(f) the industry in which the company operates – understand trends and new technologies;
(g) the competition – identify the threats;
(h) the systems – how efficient are they? Are upgrades required?
(i) legal and corporate and tax issues – is the shareholding structure robust? Are there any tax issues which need to be resolved?
(j) company contracts and leases – identify what the risks and obligations are;
(k) suppliers – are they expected to remain around?

Illustrative list of documents/information to be examined:

(i) Basic documents
Review of basic corporate documents like:

- Memorandum and Articles of Association of the Company
- Copies of Incorporation Certificate/Commencement of Business Certificate/Change of Name certificate (if applicable)
- Registered office address of the company
- History/businesses of the company
- Special rights available to any persons through shareholder or other Agreements.

(ii) Promoters/Personnel

1. Promoters' bio-data with special reference to qualification and experience. Track record of the promoters in the capital market – public issue by other group companies, violation of securities laws.

2. Directors’ & Key Personnel – details bio-data including father’s name, address, occupation, year-wise experience. Background of the Directors – including examining the list of willful defaulters periodically prepared by RBI.

3. Constitution of Audit Committee, remuneration Committee etc., Terms of reference of these committees.

4. Organization Chart.

5. Key Personnel/employees/Directors left in the last two years with reasons.

6. Break-up of employees – whether any agreement are entered into with employee – If so, copy of agreement.

7. Details of Pay scales/bonus (including performance)/PF/Gratuity etc.


(iii) Financials

1. Projections of combined operations (existing + proposed) for 5 years including the following:
   - Income details including prices
   - Cash flow and Balance Sheet
   - Capacity utilization details
   - Interest calculation – Assn. of rate/Repayment schedule
   - Depreciation – Book & I.T.
   - Tax
   - Tax etc.
   - Assumptions w.r.t. cost items
   - Commencement of commercial production (Year to be mentioned)
   - IT depreciation table for past OR (in case projections have to be
— Latest provisional accounts with all schedules
— Latest income Tax Depreciation calculation
— Input-Output ration (consumption norms) for each segment alongwith prices and input prices
— Services-wise capacity & Capacity utilization projects for the next 5 years
— Working Capital norms
— Basis for working out various expenses
— Month from which the commercial production will commence for the new project
— IT depreciation table for past.

2. Bankers to the Company – name & addresses.

3. Details of Banks Loan, Term Loan, Promissory notes, Hundis, Credit Agreements, Lease, Hire Purchase, Guarantees or any other evidences of indebtedness, Copies of Sanction letters, Original amount, Interest rate, Amount outstanding, Repayment schedule.

4. Details of default/rescheduling, if any – copy of correspondence with lenders.

5. Accounts for last 3 years and latest unaudited accounts.

6. Associate/Group Companies’ concerns accounts for last 3 years. Also give: Profile of the concerns.

7. Audited Balance Sheet, P&L Account for last 3 years of the promoter company (i.e. if promoter is a Co.)

8. In case any liabilities are not disclosed in the Balance Sheet, details thereof, or any secret reserves.

9. Age-wise analysis of stocks, debtors, creditors and loans & advances given

10. Terms of various loans & advances given

11. If names of any associates/related units are present in the debtors or parties to whom loans & advances have been given

12. Details of contingents liabilities including guarantees given by Co./directors


(iv) Project Information

1. Project Feasibility report

2. Reports/documents prepared by independent research agencies in respect of the state of the industry and demand and supply for the company’s products

3. Break-up of Cost of Project:
   — Land – Locational site & map, area, copy of documents i.e. Sale/lease Deed for land, Soil Test Report, Order for converting land into Industrial
— Building – Details break-up from Architect, Approval details from Municipality etc. and Valuation Report from a chartered engg. (for existing building and suitability of site)
— Equipments – Invoices/Quotations of main items. (Indicate Imported mach. Separately)
— Preliminary & Pre-operative expenses – break-up
— Provision for contingencies – break-up
4. Schedule of Implementation.
5. Status of Project as on a recent date – Amount spent & sources
6. Promoter’s contribution till date (supported by Auditor’s certificate if possible)
7. Current & proposed Shareholding pattern
8. Sanctions received by the issuer from bankers/institutions for debt financing in the project
   (a) Manpower
      (i) Break-up of employees – whether any agreements are entered into with employee – If so, copy of agreement
      (ii) Details of Pay scales/bonus (including performance bonus)/PF/Gratuity etc.
      (iii) Employment of contract labour – no. of workers, copy of contract.
   (b) Quality Control facilities, Research & Development.
10. Market (Demand/supply with sources alongwith copies),
11. Marketing & Distribution (network etc.) & relevant documents wherever applicable.
12. Arrangements and strategy of the company for marketing its products
13. Discussions with important customers, suppliers, Joint Venture partners, collaborators of the company.

(v) General Information
1. Details on Litigation, Disputes, overdue, statutory dues, other Material development and tax status of Company & promoters.
2. Copies of IT returns of the Company along with copies of Assessment orders for last three years.
3. Copies of IT/Wealth tax returns of the promoters along with copies of Assessment orders for last three years.
4. Copy of documents for Collaborations/Marketing Tie-ups/Other Tie-ups if any.
5. NOC/Approval/Sanctions from SEB/SPCB or copy of application.
6. Copy of SIA Registration/SSI Regn./EOU License/LOI or License.
7. Incentives if any – such as subsidy, Sales tax loans/exemption/concession/power subsidy (Copy of Booklet or notification).
8. List of existing plant & machinery with cost & age & type of ownership (lease etc.)
9. R&D (if any) cost for the project for the last three years. (Sources of any outside R&D funds including any joint venture agreements)
10. Summary of Bad Debts experience for the last five years.
11. Approvals from company’s Board of Directors/Shareholders to issue securities to the public.
13. Names of stock exchanges where shares of the Co. are listed.
14. Stock Market quotation of share, wherever applicable, as on recent date.
15. Special legislation applicable, if any, and compliance thereof (e.g. NBFCs etc.)

(vi) Third Parties
1. Brochure on collaborators, copy of Government approval for collaboration.
2. Copy of Agreement with Consultants, Copy of Government approval in case of foreign consultants.
3. Copies of important Agreements/Contracts of any sort with all the parties concerned with the company.
4. Copy of FIPB/RBI approvals (NRI/Foreign participant etc.), wherever applicable.
5. Details of Patents, Trademarks, Copyrights, Licenses etc., if any.
6. List of major customers/clients (attach copies of main pending orders).
7. Competitors & Market shares for Company’s products (with sources, wherever possible).
8. Sales arrangements, terms & conditions.

SECURITIES AND EXCHANGE BOARD OF INDIA (ISSUE OF CAPITAL AND DISCLOSURE REQUIREMENTS) REGULATIONS, 2009 (ICDR REGULATIONS)
The ICDR Regulations have been made primarily by repealing the SEBI (Disclosure and Investor Protection) Guidelines, 2000 While incorporating the provisions of the rescinded Guidelines into the ICDR Regulations, certain changes have been made by removing the redundant provisions, modifying certain provisions on account of
changes necessitated due to market design and bringing more clarity to the provisions of the rescinded Guidelines.

Applicability of ICDR Regulations
These regulations shall apply to the following:
(a) a public issue;
(b) a rights issue, where the aggregate value of specified securities offered is fifty lakh rupees or more;
(c) a preferential issue;
(d) an issue of bonus shares by a listed issuer;
(e) a qualified institutions placement by a listed issuer;
(f) an issue of Indian Depository Receipts.

Eligibility Requirements
Eligibility norms are made uniformly to all companies under SEBI (ICDR) regulations, 2009 irrespective of whether it is a banking company or infrastructure company which were given exemptions under erstwhile SEBI (DIP) Guidelines. The following are the conditions for making initial public offer
(a) The issuer has net tangible assets of at least three crore rupees in each of the preceding three full years (of twelve months each), of which not more than fifty per cent. are held in monetary assets and if more than fifty per cent. of the net tangible assets are held in monetary assets, the issuer has made firm commitments to utilise such excess monetary assets in its business or project;
(b) it has a track record of distributable profits in terms of section 205 of the Companies Act, 1956, for at least three out of the immediately preceding five years, excluding extraordinary items.
(c) it has a net worth of at least one crore rupees in each of the preceding three full years (of twelve months each);
(d) the aggregate of the proposed issue and all previous issues made in the same financial year in terms of issue size does not exceed five times its pre-issue net worth as per the audited balance sheet of the preceding financial year;
(e) if it has changed its name within the last one year, at least fifty per cent. of the revenue for the preceding one full year has been earned by it from the activity indicated by the new name.
If the above conditions are not satisfied, the issuer may make public offer, if
(a) (i) the issue is made through the book building process and the issuer undertakes to allot at least fifty per cent. of the net offer to public to qualified institutional buyers and to refund full subscription monies if it fails to make allotment to the qualified institutional buyers; or
(ii) at least fifteen per cent. of the cost of the project is contributed by scheduled commercial banks or public financial institutions, of which not less than ten per cent. shall come from the appraisers and the issuer undertakes to allot at least ten per cent. of the net offer to public to qualified institutional buyers and to refund full subscription monies if it fails to make the allotment to the qualified institutional buyers;
(b) (i) the minimum post-issue face value capital of the issuer is ten crore rupees; or
(ii) the issuer undertakes to provide market-making for at least two years from the date of listing of the specified securities, subject to the following:
(A) the market makers offer buy and sell quotes for a minimum depth of three hundred specified securities and ensure that the bid-ask spread for their quotes does not, at any time, exceed ten per cent;
(B) the inventory of the market makers, as on the date of allotment of the specified securities, shall be at least five per cent of the proposed issue.

Who is not Eligible?
(a) if the issuer, any of its promoters, promoter group or directors or persons in control of the issuer are debarred from accessing the capital market by the Board;
(b) if any of the promoters, directors or persons in control of the issuer was or also is a promoter, director or person in control of any other company which is debarred from accessing the capital market under any order or directions made by the Board;
(c) if the issuer of convertible debt instruments is in the list of wilful defaulters published by the Reserve Bank of India or it is in default of payment of interest or repayment of principal amount in respect of debt instruments issued by it to the public, if any, for a period of more than six months;
(d) unless it has made an application to one or more recognised stock exchanges for listing of specified securities on such stock exchanges and has chosen one of them as the designated stock exchange:
Provided that in case of an initial public offer, the issuer shall make an application for listing of the specified securities in at least one recognised stock exchange having nationwide trading terminals;
(e) unless it has entered into an agreement with a depository for dematerialization of specified securities already issued or proposed to be issued;
(f) unless all existing partly paid-up equity shares of the issuer have either been fully paid up or forfeited;
(g) unless firm arrangements of finance through verifiable means towards seventy five percent of the stated means of finance, excluding the amount to be raised through the proposed public issue or rights issue or through existing identifiable internal accruals, have been made.

A check list on Major IPO Compliances under SEBI(ICDR) Regulations 2009
1. Appointments of Intermediaries
   — Check whether the issuer has appointed one/more merchant bankers to carry out the obligations relating the issue?
   — Check whether the issuer has appointed SEBI registered intermediaries in consultation with lead merchant banker?
   — Check whether the issuer has appointed syndicate member in respect of issue through book building?
   — Check whether the issuer appointed registrars who has connectivity with both depositories.(ie NSDL/CDSL).
   — Ensure that the lead merchant banker is not acting as registrar to the issue in which it is also handling post issue obligations.
   — Ensure that in case of book built issue lead merchant banker and lead book runner are not different persons.
2. Filings/approvals/submissions
   — Check whether the draft offer document is filed with SEBI at least thirty days prior to registering a prospectus, red herring prospectus or shelf prospectus with ROC or filing the letter offer with the registrar of companies.
— Check whether the draft offer document is made available to the public for at least 21 days from the date of such filing with SEBI.
— Check whether a statement on the comments received from public on draft offer document is filed with SEBI.
— Ensure whether the observations/suggestions of SEBI on draft offer documents has been carried out while registering of prospectus with ROC.
— Check whether a copy of letter of offer is filed with SEBI and with stock exchanges where the securities are proposed to be listed, simultaneously while registering the prospectus with ROC /before opening of the issue.
— Check whether the company has obtained in-principle approval in respect of IPO/FPO from all the exchanges where the securities are proposed to be listed.
— Ensure whether the issuer has filed necessary documents before opening of the issue while
  a. Filing the draft offer documents with SEBI
  b. Required documents after issuance of observations by SEBI
  c. Filing of draft offer document with stock exchanges where the securities are proposed to be listed.

It may be noted that contents of offer documents hosted on Websites are the same as printed versions filed with ROC. Further the information contained in the offer document and particulars as per audited financial statements in the offer document are not more than six months old from the opening of the issue.
— Ensure that the offer document/red herring prospectus, abridged prospectus etc contain necessary disclosures.

3. Pre issue-Due Diligence Certificates
Ensure whether the lead merchant bankers has submitted due diligence certificate with SEBI at the time of
  a. filing of draft offer document with SEBI
  b. At the time of Registering prospectus with ROC
  c. Immediately before opening of the issue
  d. After the opening of the issue and before its closure before it closes for subscription.

4. Time limitation in opening of issue
Ensure that subject to compliance of Section 60(4) of the Companies Act, 1956, public/rights issue is opened within
  (i) Twelve months from the date of issuance of observations from the SEBI on draft offer document or
  (ii) Within three months from the later of the following dates if there are not observations.
  (a) Draft of Receipt of draft offer document by SEBI
  (b) Date of receipt of satisfactory reply from the lead merchant bankers, where the SEBI has sought for any clarification/information
    a. Date of receipt of clarification or information from any regulator or agency, where the SEBI has sought for any such clarification/information
    b. Date of receipt of a copy of in-principle approval letter issued by the recognized stock exchanges.
  ii. In case of Fast Track issues the issue shall be opened within 90 days from the registration of prospectus with ROC.
iii. In case of Shelf prospectus, the first issue may be opened within 3 months from the date of observation of SEBI.

5. Dispatch of offer documents and other materials
Ensure whether the offer document and other issue related instruments is dispatched to Bankers, Syndicate Members, underwriters etc in advance.

6. Underwriting for issue through book building
Ensure whether the issue through book building route is underwritten

7. Minimum Subscription
Ensure whether the company has received minimum subscription of 90% of the offer.

8. Minimum allottees
Ensure that the number of prospective allottees is at least one thousand.

9. Monitoring agency
Ensure that the issue size of more than 500 crores has been monitored by a Public Financial Institution or by one of the scheduled commercial banks named in the offer document as bankers of the issuer.

10. Time limitation for receiving the call money
Ensure the subscription money if made in calls, the outstanding subscription money is called within 12 months from the date of allotment.

11. Time limit for allotment or refund of Subscription money
Ensure that the securities are allotted and the excess amounts are refunded within 15 days from the closure of the offer.

12. Pricing
- Ensure the norms relating to price/price band, cap on price banks is complied with.
- Check whether the pricing norms are complied with respect to differential pricing
- Check whether the floor price/final price is not less than the face value of securities

13. Promoters Contribution & restriction on transferability of their securities
- Ensure that the promoters’ contribution is
  a) in case of an initial public offer, not less than twenty per cent. of the post issue capital;
  b) in case of a further public offer, either to the extent of twenty per cent. of the proposed issue size or to the extent of twenty per cent. of the post-issue capital;
  c) in case of a composite issue, either to the extent of twenty per cent. of the proposed issue size or to the extent of twenty per cent. of the post-issue capital excluding the rights issue component.
• Ensure that the promoters contribution is kept in an escrow account with a scheduled banks and shall be released to the issuer along with the release of issue proceeds.

• Ensure that the securities ineligible for promoters contribution is not included while calculating the above limits.

• Ensure that the minimum promoters contribution and excess promoters contribution is locked in for 3 years and one year respectively.

For the computation of minimum promoters’ contribution, the following specified securities(Equity Shares and Convertible Securities)shall not be eligible:

(a) specified securities acquired during the preceding three years, if they are:
   (i) acquired for consideration other than cash and revaluation of assets or capitalisation of intangible assets is involved in such transaction; or
   (ii) resulting from a bonus issue by utilisation of revaluation reserves or unrealized profits of the issuer or from bonus issue against equity shares which are ineligible for minimum promoters’ contribution;

(b) Specified securities acquired by promoters during the preceding one year at a price lower than the price at which specified securities are being offered to public in the initial public offer subject to certain exemptions specified.

(c) Specified securities allotted to promoters during the preceding one year at a price less than the issue price, against funds brought in by them during that period, in case of an issuer formed by conversion of one or more partnership firms, where the partners of the erstwhile partnership firms are the promoters of the issuer and there is no change in the management:

(d) Specified securities pledged with any creditor.

14. Other lock in requirements

• Ensure that the pre-issue capital held by persons other than promoters is subject to lockin for the period of one year from the date of allotment, subject to specified exemptions.

• Transferability of lock in shares

   Subject to the provisions of Securities and Exchange Board of India (Substantial Acquisition of shares and Takeovers) Regulations, 1997, the specified securities held by promoters and locked-in may be transferred to another promoter or any person of the promoter group or a new promoter or a person in control of the issuer and

   the specified securities held by persons other than promoters and locked-in may be transferred to any other person holding the specified
securities which are locked-in along with the securities proposed to be transferred:
However, lock-in on such specified securities shall continue for the remaining period with the transferee and such transferee shall not be eligible to transfer them till the lock-in period stipulated in these regulations has expired.

15. Minimum offer to the Public

Subject to the provisions of sub-clause (b) of clause (2) of rule 19 of Securities Contracts (Regulations) Rules, 1957, check the net offer to public:
(a) in case of an initial public offer, is at least ten per cent. or twenty five per cent. of the post-issue capital, as the case may be; and
(b) in case of a further public offer, is at least ten per cent. or twenty five per cent. of the issue size, as the case may be.

However Government companies and infrastructure Companies are exempted from these provisions subject to exceptions.

16. Reservation on Competitive Basis

• For issue made through the book building process
(1) In case of an issue made through the book building process, the issuer may make reservation on competitive basis out of the issue size excluding promoters’ contribution and net offer to public in favour of the following categories of persons:
(a) employees of the issuer including employees of the promoting companies in case of a new issuer;
(b) shareholders (other than promoters) of:
   (i) listed promoting companies, in case of a new issuer; and
   (ii) listed group companies, in case of an existing issuer:
(c) persons who, as on the date of filing the draft offer document with the Board, are associated with the issuer as depositors, bondholders or subscribers to services of the issuer making an initial public offer:

• For issue made other than through the book building process
In case of an issue made other than through the book building process, the issuer may make reservation on competitive basis out of the issue size excluding promoters’ contribution and net offer to public in favour of the following categories of persons:
(a) employees of the issuer including employees of the promoting companies in case of a new issuer;
(b) shareholders (other than promoters) of:
   (i) listed promoting companies, in the case of a new issuer; and
   (ii) listed group companies, in the case of an existing issuer:
- Ensure that reservations have not been made in respect of the following persons who are not eligible.
  
a. In case of promoting companies being financial institutions or state and central financial institutions, the shareholders of such promoting companies

b. In case of issue made through book building process, the issue management team, syndicate members, their promoters, directors and employees and for the group or associate companies of the issue management team and syndicate members and their promoters, directors and employees;

16. Allocation of net offer to public

In case of issue through book building

i. Not less than 35% to Retail individual investors
ii. Not less than 15% to non-institutional investors
iii. Nor more than 55% to qualified institutional buyers and 5% of which shall be allocated to mutual funds. (up to 35% of the portion available for allocation of qualified institutional buyers may be allocated to anchor investor)

However at least 50% of net offer is to be allocated to qualified institutional buyers if an issuer has not satisfied the basic eligibility criteria and undertakes to allot so. Further if the issuer is required to allot 60% of the net offer to the public to Qualified institutional Buyers in terms of 19(2)(b) of Securities Contracts Regulation Rules, 1957, allocation to retail individual investors and non institutional investors shall be 30% and 10% respectively.

In case of issue other than book building

i. Minimum 50% to retail individual investors and
ii. Remaining to individual applicants other than retail individual investors and
   Other investors including corporate bodies or institutions, irrespective of the number of securities applied for.

17. Period of subscription

Ensure that the public issue is kept open at least for three working days but not more than ten working days including the days for which the issue is kept open in case of revision in price band.

18. Advertisements

- Pre issue
  Ensure that after registering the red herring prospectus (in case of a book built issue) or prospectus (in case of fixed price issue) with the Registrar of Companies, make a pre-issue advertisement in the prescribed format and with required disclosures, in one English national daily newspaper with wide circulation, Hindi national daily
newspaper with wide circulation and one regional language newspaper with wide circulation at the place where the registered office of the issuer is situated.

- **Issue opening and closing**

Ensure that the advertisement on issue opening and closing is made in the specified format.

- **Post issue advertisement**

Ensure that advertisement giving details relating to oversubscription, basis of allotment, number, value and percentage of all applications including ASBA, number, value and percentage of successful allottees for all applications including ASBA, date of completion of dispatch of refund orders or instructions to Self Certified Syndicate Banks by the Registrar, date of dispatch of certificates and date of filing of listing application, etc. is released within ten days from the date of completion of the various activities in at least one English national daily newspaper with wide circulation, one Hindi national daily newspaper with wide circulation and one regional language daily newspaper with wide circulation at the place where registered office of the issuer is situated.

Major issues to be taken care while issuing advertisement/publicity material

- Ensure that issuer, advisors, brokers or any other entity connected with the issue do not publish any advertisement stating that issue has been oversubscribed or indicating investors' response to the issue, during the period when the public issue is still open for subscription by the public.
- Ensure that all public communications and publicity material issued or published in any media during the period commencing from the date of the meeting of the board of directors of the issuer in which the public issue or rights issue is approved till the date of filing draft offer document with the Board is consistent with its past practices
- Ensure that any public communication including advertisement and publicity material issued by the issuer or research report made by the issuer or any intermediary concerned with the issue or their associates contains only factual information and does not contain projections, estimates, conjectures, etc. or any matter extraneous to the contents of the offer document
- Ensure that the announcement regarding closure of the issue is made only after the receipt of minimum subscription.
- Ensure that no product advertisement contains any reference, directly or indirectly, to the performance of the issuer during the period commencing from the date of the resolution of the board of directors of the issuer approving the public issue or rights issue till the date of allotment of specified securities offered in such issue.
- Ensure that no advertisement or distribution material with respect to the issue contains any offer of incentives, whether direct or indirect, in any manner, whether in cash or kind or services or otherwise.
- Ensure that the advertisement does not include any issue slogans or brand names for the issue except the normal commercial name of the issuer or commercial brand names of its products already in use
19. **Minimum Application Value**
Ensure that Minimum application Value is kept between Rs.5000 to Rs. 7000

20. **Allotment procedure and basis of allotment**
The allotment of specified securities to applicants other than anchor investors shall be on proportionate basis within the specified investor categories and the number of securities allotted shall be rounded off to the nearest integer, subject to minimum allotment being equal to the minimum application size as determined and disclosed by the issuer

21. **Appointment of Compliance officer**
The issuer shall appoint a compliance officer who shall be responsible for monitoring the compliance of the securities laws and for redressal of investors’ grievances.

21. **Redressal of investor grievances**
The post-issue lead merchant bankers shall actively associate himself with post-issue activities such as allotment, refund, despatch and giving instructions to syndicate members, Self Certified Syndicate Banks and other intermediaries and shall regularly monitor redressal of investor grievances arising therefrom.

24. **Post issue diligence**
(1) The lead merchant bankers shall exercise due diligence and satisfy himself about all the aspects of the issue including the veracity and adequacy of disclosure in the offer documents.
(2) The lead merchant bankers shall call upon the issuer, its promoters or directors or in case of an offer for sale, the selling shareholders, to fulfil their obligations as
disclosed by them in the offer document and as required in terms of these Regulations.

(3) The post-issue merchant banker shall continue to be responsible for post-issue activities till the subscribers have received the securities certificates, credit to their demat account or refund of application moneys and the listing agreement is entered into by the issuer with the stock exchange and listing/trading permission is obtained.

(4) The responsibility of the lead merchant banker shall continue even after the completion of issue process.

23. Post issue Reports
The lead merchant banker shall submit post-issue reports as follows:
(a) initial post issue report in specified form within three days of closure of the issue
(b) final post issue report in specified format within fifteen days of the date of finalisation of basis of allotment or within fifteen days of refund of money in case of failure of issue. The lead merchant banker shall also submit a due diligence certificate in the specified format along with the final post issue report.

ROLE OF COMPANY SECRETARY IN AN IPO

The Securities Exchange Board of India Act, 1992 (SEBI Act) was formed, inter alia, to provide for the establishment of a Board (SEBI) to protect the interest of investors in securities and to promote the development of and to regulate the securities market.

SEBI regulates the securities market by prescribing measures to register and regulate the working of Capital Market Intermediaries associated with Securities market. Such intermediaries undertake following major activities relating to securities in addition to other activities:
— Management of an Issue of Capital
— Manager of Co-manager
— Advisor to issue
— Corporate Advisory Services
— Underwriting
— Registrar to an Issue and Share Transfer Agent
— Private Placement
— Public announcement and offer documents for acquisition of shares under Takeover code
— Portfolio Manager
— Brokers, Sub-brokers.

The main role of these Capital Market Intermediaries is to provide maximum information to the investors by means of disclosures carrying vital information. The intermediaries are necessarily compelled to associate with other professionals to advise the compliance of the Act, rules and regulations, notifications, guidelines, instructions, etc., directly by the Board or the Central Government to point out the non-compliance and ensure the complete compliance. In a capital market issue, the major role in synchronizing these activities of intermediaries lies with a qualified
Company Secretary.

Section 2(2) of the Company Secretaries Act, 1980 indicates the various areas of practice which are open to a Company Secretary holding certificate of practice issued by the Institute. The objective of authorizing members to practice is to make available professional services of a Company Secretary to the corporate sector.

The educational background, knowledge, training and exposure that a company secretary acquires makes him a versatile professional capable of rendering a wide range of services to companies of all sizes, other commercial and industrial organizations; including small and medium sized companies which are not required by law, to employ compulsorily a Whole-Time Company Secretary.

The plethora of services, which a Practising Company Secretary can render in IPOs can be listed as under:

1. Planning Stage
   (a) Deciding the time line
   (b) Compliance related issues
   (c) Importance of Corporate Governance
   (d) Structure of Board
   (e) Promoters consent
   (f) Method of issuance of shares (Demat/Physical/Both) - Compliance

2. Due diligence
   (a) Company Contract and Leases
   (b) Legal and Tax Issues
   (c) Corporate issues
   (d) Financial Assets
   (e) Financial Statement
   (f) Creditors & Debtors
   (g) Legal Cases against the company

3. Appointing Advisors and other intermediaries such as:
   (a) Investment Bankers
   (b) Book Running Lead Managers
   (c) Issues with Depository
   (d) Legal Advisor
   (e) Bankers

4. Offer Document
   (a) Drafting the offer document
   (b) Filing with SEBI
   (c) In-principle approval of Stock Exchange
(d) Filing with Designated Stock Exchanges
(e) Complying with Comments received from SEBI
(f) Filing with ROC

5. Issue Period
(a) Adhering to Issue Opening/Closing Date
(b) Compiling Field Reports on subscription status
(c) Coordinating with Registrar/Bankers to the issue

6. Allotment of shares
(a) Basis of allotment
(b) Board meeting for allotment
(c) Crediting shares in beneficiary account/dispatch of share certificates
(d) Despatch of refund orders
(e) Payment of stamp duty

7. Listing
(a) Filing for Listing with Designated Stock Exchange
(b) Finalisation of Listing Process

8. Post issue compliances
(a) To ensure proper compliance with Listing Agreement
(b) Redressal of shareholder complaints
(c) Timely filing of required reports with ROC/SEBI/Stock Exchange

As can be seen from the above, a Company Secretary is a key member in an IPO team. Apart from checking the applicability and eligibility norms or exemption from eligibility norms and the pre-listing requirements of Stock Exchange, he is responsible for ensuring that the company has complied with the pre-issue, issue and post-issue obligations of the company and corporate governance requirements including disclosures with respect to, inter alia, material contracts, statutory approvals, subsidiaries and promoter holding and litigations.

Compliance of SEBI (ICDR) Regulation 2009 and other applicable Acts and guidelines is a primary responsibility of the Company Secretary in case the company proposes to list its securities abroad, he is also required to comply with conditions for listing abroad.

III. DUE DILIGENCE – ISSUES OTHER THAN IPO/FPO

Companies might issue shares through routes other than IPO/FPO. It right include preferential allotments, issue of shares through rights issue, bonus issue or ESOP scheme etc. various important aspects to be taken case before and after the issue are diseased below.

III-A. DUE DILIGENCE – PREFERENTIAL ISSUE
Due diligence of preferential issue may be
(a) Due diligence of preferential issues by listed companies.
(b) Due diligence of preferential issues by unlisted companies.

Due diligence of preferential issues by listed companies
a. Due Diligence Preferential issue of listed Companies - a Check list under Chapter VII of SEBI(ICDR) Regulations 2009

Non Applicability
1. The provisions of this Chapter shall not apply where the preferential issue of equity shares is made:
(a) pursuant to conversion of loan or option attached to convertible debt instruments in terms of sub-sections (3) and (4) of sections 81 of the Companies Act, 1956;
(b) pursuant to a scheme approved by a High Court under section 391 to 394 of the Companies Act, 1956;
(c) in terms of the rehabilitation scheme approved by the Board of Industrial and Financial Reconstruction under the Sick Industrial Companies (Special Provisions) Act, 1985:
Provided that the lock-in provisions of this Chapter shall apply to such preferential issue of equity shares.

(2) The provisions of this Chapter relating to pricing and lock-in shall not apply to equity shares allotted to any financial institution within the meaning of sub-clauses (ia) and (ii) of clause (h) of section 2 of the Recovery of Debts due to Banks and Financial Institutions Act, 1993 (51 of 1993).

(3) The provisions of regulation 73 (Disclosures) and regulation 76 (Pricing) shall not apply to a preferential issue of equity shares and compulsorily convertible debt instruments, whether fully or partly, where the Board has granted relaxation to the issuer in terms of regulation 29A of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 1997, if adequate disclosures about the plan and process proposed to be followed for identifying the allottees are given in the explanatory statement to notice for the general meeting of shareholders.

Check list for preferential issue of listed companies
1. Special Resolution
   • Check whether a special resolution has been passed by its shareholders;
   • The special resolution shall specify the relevant date on the basis of which price of the equity shares to be allotted on conversion or exchange of convertible securities shall be calculated

"relevant date" means:
(a) in case of preferential issue of equity shares, the date thirty days prior to the date on which the meeting of shareholders is held to consider the proposed preferential issue:
Provided that in case of preferential issue of equity shares pursuant to a scheme approved under the Corporate Debt Restructuring framework of Reserve Bank of India, the date of approval of the Corporate Debt Restructuring Package shall be the relevant date.

(b) in case of preferential issue of convertible securities, either the relevant date referred to in clause (a) of this regulation or a date thirty days prior to the date on which the holders of the convertible securities become entitled to apply for the equity shares.

- The issuer shall, in addition to the disclosures required under section 173 of the Companies Act, 1956 or any other applicable law, disclose the following in the explanatory statement to the notice for the general meeting proposed for passing special resolution:
  (a) the objects of the preferential issue;
  (b) the proposal of the promoters, directors or key management personnel of the issuer to subscribe to the offer;
  (c) the shareholding pattern of the issuer before and after the preferential issue;
  (d) the time within which the preferential issue shall be completed;
  (e) the identity of the proposed allottees, the percentage of post preferential issue capital that may be held by them and change in control, if any, in the issuer consequent to the preferential issue;
  (f) an undertaking that the issuer shall re-compute the price of the specified securities in terms of the provision of these regulations where it is required to do so;
  (g) an undertaking that if the amount payable on account of the re-computation of price is not paid within the time stipulated in these regulations, the specified securities shall continue to be locked-in till the time such amount is paid by the allottees.

2. Compulsory Dematerialisation
Check whether all the equity shares, if any, held by the proposed allottees in the issuer are in dematerialised form;

3. Condition for continued listing
Check the issuer is in compliance with the conditions for continuous listing of equity shares as specified in the listing agreement

4. Permanent Account Number of allottees
Check whether the issuer has obtained the Permanent Account Number of the proposed allottees.

5. Shares not to be allotted to persons who has sold any equity shares of the issuer in preceding six months
Ensure that the issuer has not make preferential issue of specified securities to any person who has sold any equity shares of the issuer during the six months preceding the relevant date: However, in respect of the preferential issue of equity shares and compulsorily convertible debt instruments, whether fully or partly, the Board may grant relaxation from the requirements of this sub-regulation, if the Board has granted
relaxation in terms of regulation 29A of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 to such preferential allotment.

6. Copy of the certificate of its statutory auditor
The issuer shall place a copy of the certificate of its statutory auditor before the general meeting of the shareholders, considering the proposed preferential issue, certifying that the issue is being made in accordance with the requirements of these regulations.

7. Valuation by an independent qualified valuer
Where specified securities are issued on a preferential basis to promoters, their relatives, associates and related entities for consideration other than cash, the valuation of the assets in consideration for which the equity shares are issued shall be done by an independent qualified valuer, which shall be submitted to the recognised stock exchanges where the equity shares of the issuer are listed: If the recognised stock exchange is not satisfied with the appropriateness of the valuation, it may get the valuation done by any other valuer and for this purpose it may obtain any information, as deemed necessary, from the issuer.

8. Time Limit for allotment.

Allotment pursuant to the special resolution shall be completed within a period of fifteen days from the date of passing of such resolution:

Exceptions
Where any application for exemption from the applicability of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 or any approval or permission by any regulatory authority or the Central Government for allotment is pending, the period of fifteen days shall be counted from the date of order on such application or the date of approval or permission, as the case may be:

Where the Board has granted relaxation to the issuer in terms of regulation 29A of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997, the preferential issue of equity shares and compulsorily convertible debt instruments, whether fully or partly, shall be made by it within such time as may be specified by the Board in its order granting the relaxation:

Requirement of allotment within fifteen days shall not apply to allotment of specified securities on preferential basis pursuant to a scheme of corporate debt restructuring as per the corporate debt restructuring framework specified by the Reserve Bank of India.

(2) If the allotment of specified securities is not completed within fifteen days from the date of special resolution, a fresh special resolution shall be passed and the relevant date for determining the price of specified securities under this Chapter will be taken with reference to the date of latter special resolution.
The tenure of the convertible securities of the issuer shall not exceed eighteen months from the date of their allotment.

a. If listed for more than 6 months
If the equity shares of the issuer have been listed on a recognised stock exchange for a period of six months or more as on the relevant date, the equity shares shall be allotted at a price not less than higher of the following:
(a) The average of the weekly high and low of the closing prices of the related equity shares quoted on the recognised stock exchange during the six months preceding the relevant date; or
(b) The average of the weekly high and low of the closing prices of the related equity shares quoted on a recognised stock exchange during the two weeks preceding the relevant date.

b. If listed for less than 6 months
If the equity shares of the issuer have been listed on a recognised stock exchange for a period of less than six months as on the relevant date, the equity shares shall be allotted at a price not less than the higher of the following:

(a) the price at which equity shares were issued by the issuer in its initial public offer or the value per share arrived at in a scheme of arrangement under sections 391 to 394 of the Companies Act, 1956, pursuant to which the equity shares of the issuer were listed, as the case may be;

or

(b) the average of the weekly high and low of the closing prices of the related equity shares quoted on the recognised stock exchange during the period shares have been listed preceding the relevant date; or

(c) the average of the weekly high and low of the closing prices of the related equity shares quoted on a recognised stock exchange during the two weeks preceding the relevant date.

This price shall be recomputed by the issuer on completion of six months from the date of listing on a recognised stock exchange with reference to the average of the weekly high and low of the closing prices of the related equity shares quoted on the recognised stock exchange during these six months and if such recomputed price is higher than the price paid on allotment, the difference shall be paid by the allottees to the issuer.
c. Preferential issue to qualified institutional buyer
Any preferential issue of specified securities, to qualified institutional buyers not exceeding five in number, shall be made at a price not less than the average of the weekly high and low of the closing prices of the related equity shares quoted on a recognised stock exchange during the two weeks preceding the relevant date.

‘stock exchange’ means any of the recognised stock exchanges in which the equity shares are listed and in which the highest trading volume in respect of the equity shares of the issuer has been recorded during the preceding six months prior to the relevant date.

11. Payment of consideration.
Full consideration of specified securities other than warrants issued under this Chapter shall be paid by the allottees at the time of allotment of such specified securities:

Exceptions
In case of a preferential issue of specified securities pursuant to a scheme of corporate debt restructuring as per the corporate debt restructuring framework specified by the Reserve Bank of India, the allottee may pay the consideration in terms of such scheme.

An amount equivalent to at least twenty five per cent. of the consideration shall be paid against each warrant on the date of allotment of warrants. The balance seventy five per cent. of the consideration shall be paid at the time of allotment of equity shares pursuant to exercise of option against each such warrant by the warrant holder.

In case the warrant holder does not exercise the option to take equity shares against any of the warrants held by him, the consideration paid in respect of such shall be forfeited by the issuer.

12. Lock-in of specified securities.
- The specified securities allotted on preferential basis to promoter or promoter group and the equity shares allotted pursuant to exercise of options attached to warrants issued on preferential basis to promoter or promoter group, shall be locked-in for a period of three years from the date of allotment of the specified securities or equity shares allotted pursuant to exercise of the option attached to warrant, as the case may be:

Exceptions/Conditions

Not more than twenty per cent of the total capital of the issuer shall be locked-in for three years from the date of allotment:

Equity shares allotted in excess of the twenty per cent. shall be locked-in for one year from the date of their allotment pursuant to exercise of options or otherwise, as the case may be.
• The specified securities allotted on preferential basis to persons other than promoter and promoter group and the equity shares allotted pursuant to exercise of options attached to warrants issued on preferential basis to such persons shall be locked in for a period of one year from the date of their allotment.

• The lock-in of equity shares allotted pursuant to conversion of convertible securities other than warrants, issued on preferential basis shall be reduced to the extent the convertible securities have already been locked-in.

• The equity shares issued on preferential basis pursuant to a scheme of corporate debt restructuring as per the Corporate Debt Restructuring framework specified by the Reserve Bank of India shall be locked-in for a period of one year from the date of allotment: However partly paid up equity shares, if any, shall be locked-in from the date of allotment and the lock-in shall end on the expiry of one year from the date when such equity shares become fully paid up.

If the amount payable by the allottee, in case of re-calculation of price after completion of six months from the date of listing, is not paid till the expiry of lock-in period, the equity shares shall continue to be locked in till such amount is paid by the allottee.

• The entire pre-preferential allotment shareholding of the allottees, if any, shall be locked-in from the relevant date upto a period of six months from the date of preferential allotment.

13. Transferability of locked-in specified securities and warrants issued on preferential basis.

Subject to the provisions of Securities and Exchange Board of India (Substantial Acquisition of shares and Takeovers) Regulations, 1997, specified securities held by promoters and locked-in may be transferred among promoters or promoter group or to a new promoter or persons in control of the issuer:

Provided that lock-in on such specified securities shall continue for the remaining period with the transferee.

Due diligence – Preferential issues of unlisted companies

Issue of preferential allotments by unlisted companies is mainly governed by Unlisted Public Companies (Preferential Allotment) Rules, 2003. These rules are applicable to all unlisted public companies in respect of preferential issue of equity shares, fully convertible debentures, partly convertible debentures or any other financial instruments which would be convertible into or exchanged with equity shares at a later date.

The following check list provides the details of compliances by unlisted companies.

(i) Check whether there is a provision in the Articles of Association authorizing the Board to make preferential allotment.

(ii) Check whether there is adequate unissued capital

(iii) Ensure to pass necessary special resolution under Section 81(1A) of the Companies Act, 1956 and necessary filings with ROC
(iv) Ensure that the explanatory statement to the notice for the general meeting as required under section 173 of the Companies Act, 1956 contains the following:

(a) the price or price band at which the allotment is proposed;
(b) the relevant date on the basis of which price has been arrived at;
(c) the object/s of the issue through preferential offer;
(d) the class or classes of persons to whom the allotment is proposed to be made;
(e) intention of promoters/directors/key management persons to subscribe to the offer;
(f) shareholding pattern of promoters and others classes of shares before and after the offer;
(g) proposed time within which the allotment shall be completed;
(h) whether a change in control is intended or expected

(v) Ensure that, in case of every issue of shares/warrants/fully convertible debentures/partly convertible debentures or other financial instruments with conversion option, the statutory auditors of the issuing company / company secretary in practice certifies that the issue of the said instruments is being made in accordance with these Rules and such certificate is being laid before the meeting of the shareholders convened to consider the proposed issue.

(vi) Ensure to complete the allotment within 12 months of passing special resolution

(vii) Ensure to make necessary filings with ROC in respect of the said preferential allotment.

III-B. DUE DILIGENCE – EMPLOYEE STOCK OPTION

Issue of shares through Employee Stock Option Scheme/Employee Stock Purchase scheme by listed companies are regulated by Securities And Exchange Board of India (Employee Stock Option Scheme and Employee Stock Purchase Scheme) Guidelines, 1999. The following aspects are to be checked while issue of shares/options to employees under ESOP scheme.

(a) Employee Stock Option

1. Eligibility to Participate

(i) An employee is eligible to participate in Employee Stock Option Scheme (ESOS) of the company.

Where such employee is a director nominated by an institution as its representative on the Board of Directors of the company—

(ii) the contract/agreement entered into between the institution nominating its employee as the director of a company and the director so appointed shall, inter alia, specify the following:

(a) whether options granted by the company under its ESOS can be accepted by the said employee in his capacity as director of the...
(b) that options, if granted to the director, shall not be renounced in favour of the nominating institution; and

(c) the conditions subject to which fees, commissions, ESOSs, other incentives, etc. can be accepted by the director from the company.

(ii) the institution nominating its employee as a director of a company shall file a copy of the contract/agreement with the said company, which shall, in turn, file the copy with all the stock exchanges on which its shares are listed.

(iii) the director so appointed shall furnish a copy of the contract/agreement at the first Board meeting of the company attended by him after his nomination.

(ii) Check that employee is not a promoter nor belongs to the promoter group.

(ii) Check that a director who either himself or through his relative or through any body corporate, directly or indirectly holds more than 10% of the outstanding equity shares of the company is not participating as he is not eligible to participate in the scheme.

2. Compensation Committee

(i) Check that the disclosures, as specified in Schedule IV are made by the company to the prospective option guarantees.

(ii) Check that the company has constituted a Compensation Committee for administration and superintendence of the scheme.

(iii) Check that the Compensation Committee is a Committee of the Board of Directors consisting of a majority of independent directors.

(iv) Check that the Compensation Committee has formulated the detailed terms and conditions of the scheme including:

(a) the quantum of option to be granted under the scheme per employee and in aggregate;

(b) the conditions under which option vested in employees may lapse in case of termination of employment for misconduct;

(c) the exercise period within which the employee should exercise the option and that option would lapse on failure to exercise the option within the exercise period;

(d) the specified time period within which the employee shall exercise the vested options in the event of termination or resignation of an employee;

(e) the right of an employee to exercise all the options vested in him at one time or at various points of time within the exercise period;

(f) the procedure for making a fair and reasonable adjustment to the number of options and to the exercise price in case of corporate actions such as rights issues, bonus issues, merger, sale of division and others. In this regard, the following actions should be taken into consideration by the compensation Committee:
(i) The number and the price of ESOS shall be adjusted in a manner such that total value of ESOS remains the same after the corporate action.

(ii) For this purpose global best practices in this area including the procedures followed by the derivatives markets in India and abroad shall be considered.

(iii) The vesting period and the life of the options shall be left unaltered as far as possible to protect the rights of option holders.

(g) the grant, vest and exercise of option in case of employees who are on long leave; and

(h) the procedure for cashless exercise of options.

(v) Check that suitable policies and systems have been framed by the compensation committee to ensure that there is no violation of the following by any employee—

(a) Securities and Exchange Board of India (Insider Trading) Regulations, 1992; and


3. Shareholders’ Approval

(i) Check that the approval of shareholders of the company has been obtained by passing a special resolution in general meeting.

(ii) Check that the explanatory statement to the notice and the resolution proposed to be passed in general meeting for scheme containing the following information has also been sent:

(a) the total number of options to be granted;

(b) identification of classes of employees entitled to participate in the scheme;

(c) requirements of vesting and period of vesting;

(d) maximum period within which the option shall be vested;

(e) exercise price or pricing formula;

(f) exercise period and process of exercise;

(g) the appraisal process for determining the eligibility of employees to the scheme;

(h) maximum number of options to be issued per employee and in aggregate;

(i) a statement to the effect that the company shall conform to the accounting policies specified by SEBI in regard to ESOS;

(j) the method which the company uses to value its options, i.e., whether fair value or intrinsic value.
(k) in case the company calculates the employees compensation cost using the intrinsic value of the stock options, the difference between the employees compensation cost so computed and employee compensation cost that shall have been recognized, if it had used the fair value of the options, shall be disclosed in the directors report and also the impact of this difference on profits and on EPS of the company shall be disclosed in directors report.

(iii) Check that approval of shareholders by way of a separate resolution in the general meeting has been obtained by company in case of—

(a) grant of option to employees of subsidiary or holding company and,

(b) grant of option to identified employees, during any one year, equal to or exceeding 1% of the issued capital (excluding outstanding warrants and conversions) of the company at the time of grant of option.

4. Variation of Terms of ESOS

(i) Check that the company does not vary the terms of the Scheme in any manner which may be detrimental to the interests of the employees.

(ii) However, if such variation is not prejudicial to the interests of the option holders, Check that the company has passed a special resolution in a general meeting to vary the terms of scheme.

(iii) the provisions of clause 3(iii) as above shall apply to such variation of terms as they apply to the original grant of option.

(iv) Check that the notice for passing special resolution for variation of terms of ESOS has been sent.

(v) Check that the notice discloses full details of the variation, the rationale therefor and the details of the employees who are beneficiary of such variation.

(vi) The companies have been given an option to reprice the options which are not exercised if ESOSs were rendered unattractive due to fall in the price of shares in the market. The company must ensure that such re-pricing should not be detrimental to the interest of employees and approval of shareholders in General Meeting has been obtained for such pricing.

5. Pricing

The companies granting option to its employees pursuant to the scheme have the freedom to determine the exercise price subject to adherence to the accounting policies. In case the company calculates the employee compensation cost using the intrinsic value of the stock options, the difference between the employee compensation cost so computed and the employee compensation cost that shall have been recognized if it had used the fair value of the options, is required to be disclosed in the Director’s Report and also the impact of this difference on profits and on Earnings per Share of the company shall also be disclosed in the Director’s Report.

6. Lock-in-Period and Rights of the Option-holder
(i) Check that there exists a minimum period of one year between the grant of options and vesting of option. Also ensure that, in a case where options are granted by a company under an ESOS in lieu of options held by the same person under an ESOS in another company which has merged or amalgamated with the first mentioned company, the period during which the options granted by the transferor company were held by him shall be adjusted against the minimum vesting period required under this clause.

(ii) The company has the freedom to specify the lock-in-period for the shares issued pursuant to exercise of option.

(iii) Check that the employee does not have the right to receive any dividend or to vote or in any manner enjoys the benefits of a shareholder in respect of option granted to him, till shares are issued on exercise of option.

7. Consequence of Failure to Exercise Option

(i) Check that amount payable by the employee, if any, at the time of grant of option has been forfeited by the company if the option is not exercised by the employee within the exercise period; or

(ii) Check that the amount has been refunded to the employee if the option is not vested due to non-fulfilment of condition relating to vesting of option as per the Scheme.

8. Non-Transferability of Option

(i) Check that option granted to an employee is not transferable to any person.

(ii) (a) No person other than the employee to whom the option is granted shall be entitled to exercise the option.

(b) under the cashless system of exercise, the company may itself fund or permit the empanelled stock brokers to fund the payment of exercise price which shall be adjusted against the sale proceeds of some or all the shares, subject to the provisions of the Companies Act, 1956.

(iii) Check that the option granted to the employee is not pledged, hypothecated, mortgaged or otherwise alienated in any other manner.

(iv) Check that in the event of the death of employee while in employment, all the options granted to him till such date are vested in the legal heirs or nominees of the deceased employee.

(v) Check that in case the employee suffers a permanent incapacity while in employment, all the option granted to him as on the date of permanent incapacitation, shall vest in him on that day.

(vi) Check that if an employee resigns or is terminated, all options not vested as on that day expire. However, the employee shall, subject to the terms and conditions formulated by compensation committee, be entitled to retain all the vested options.

(vii) Check that, the options granted to a director, who is an employee of an institution and has been nominated by the said institution, has not been renounced in favour of institution nominating him.

1. Check that the Board of Directors disclose either in the Directors Report or in the Annexure to the Director’s Report, the following details of the Scheme:

   (a) options granted;
   (b) the pricing formula;
   (c) options vested;
   (d) options exercised;
   (e) the total number of shares arising as a result of exercise of option;
   (f) options lapsed;
   (g) variation of terms of options;
   (h) money realized by exercise of options;
   (i) total number of options in force;
   (j) employee-wise details of options granted to—
      (i) senior managerial personnel;
      (ii) any other employee who receives a grant in any one year of option amounting to 5% or more of option granted during that year;
      (iii) identified employees who were granted option, during any one year, equal to or exceeding 1% of the issued capital (excluding outstanding warrants and conversions) of the company at the time of grant;
   (k) diluted Earnings Per Share (EPS) pursuant to issue of shares on exercise of option calculated in accordance with International Accounting Standard (IAS) 33.
   (l) Where the company has calculated the employee compensation cost using the intrinsic value of the stock options, the difference between the employee compensation cost so computed and the employee compensation cost that shall have been recognized if it had used the fair value of the options, shall be disclosed. The impact of this difference on profits and on EPS of the company shall also be disclosed.
   (m) Weighted-average exercise prices and weighted-average fair values of options shall be disclosed separately for options whose exercise price either equals or exceeds or is less than the market price of the stock.
   (n) A description of the method and significant assumptions used during the year to estimate the fair values of options, including the following weighted average information:
      (1) risk-free interest rate,
      (2) expected life,
      (3) expected volatility,
      (4) expected dividends, and
      (5) the price of the underlying share in market at the time of option grant.
2. Ensure that until all options granted in the three years prior to the IPO have been exercised or have lapsed, disclosures are made either in the Directors’ Report or in an Annexure thereto of the information specified above in respect of such options also.

3. Ensure that until all options granted in the three years prior to the IPO have been exercised or have lapsed, disclosure are made either in the Directors’ Report or in an Annexure thereto of the impact on the profits and on the EPS of the company if the company had followed the accounting policies specified under clause 13 of these guidelines in respect of such options.

10. Accounting Policies

Check that the company which has passed a resolution for the scheme complies with the accounting policies specified by SEBI in regard to the Scheme under Schedule I of the SEBI (Employee Stock Option Scheme and Employee Stock Purchase Scheme) Guidelines, 1999.

11. Certificate from Auditors

Check that the Board of Directors of company present before the shareholders at each AGM, a certificate from the auditors of the company that the Scheme has been implemented in conformity with these guidelines and in accordance with the resolution of the company in the general meeting.

(b) Employees Stock Purchase Scheme (ESPS)

1. Eligibility to Participate in the Scheme

   (i) An employee eligible to participate in the scheme should be:

      (a) a permanent employee of the company working in India or out of India; or

      (b) a director of the company, whether a whole time director or not;

      (c) an employee as defined in sub-clauses (a) or (b) of a subsidiary, in India or out of India, or of a holding company of the company.

   (ii) Check that the employee is not a promoter nor belongs to the promoter group.

   (iii) Ensure that a director who either by himself or through his relatives or through any body corporate, directly or indirectly holds more than 10% of the outstanding equity shares of the company is not participating, as he is not eligible to participate in the scheme.

2. Shareholder Approval

   (i) Check that the Scheme has been approved by the shareholders by passing a special resolution in the meeting of the general body of shareholders.

   (ii) Check that the explanatory statement to the notice has been sent to the shareholders and it specifies—

      (a) the price of the shares and also the number of shares to be offered to each employee;
(b) the appraisal for determining the eligibility of employee for the scheme;
(c) total number of shares to be issued.

(iii) The number of shares offered may be different for different categories of employees.

(iv) Check that special resolution states that the company shall conform to the accounting policies as specified in Schedule II of the SEBI (Employee Stock Option Scheme and Stock Purchase Scheme) Guidelines, 1999.

(v) Check that approval of shareholders have been obtained by way of separate resolution in the general meeting in case of—
   (a) allotment of shares to employees of subsidiary or holding company and;
   (b) allotment of shares to identified employees, during any one year, equal to or exceeding 1% of the issued capital (excluding outstanding warrants and conversions) of the company at the time of allotment of shares.

3. Pricing and Lock-in-period

(i) The company has the freedom to determine price of shares to be issued under an ESPS, provided they comply with the accounting policies specified.

(ii) Check that the shares issued under an ESPS are subject to lock-in for a minimum period of one year from the date of allotment.

   Also ensure that in a case where shares are allotted by a company under an ESPS in lieu of shares acquired by the same person under an ESPS in another company which has merged or amalgamated with the first mentioned company, the lock-in-period already undergone in respect of shares of the transferor company shall be adjusted against the lock-in required under this clause.

(iii) If the scheme is part of a public issue and the shares are issued to employees at the same price as in the public issue, the shares issued to employees under the scheme are not subject to any lock-in-period.

4. Disclosure and Accounting Policies

(i) Check that the Director’s Report or Annexure thereto shall contain, inter alia, the following disclosures:

   (a) the details of the number of shares issued in the scheme;
   (b) the price at which such shares are issued;
   (c) employee-wise details of the shares issued to:
      (i) senior managerial personnel;
      (ii) any other employee who is issued shares in any one year amounting to 5% or more shares issued during that year;
      (iii) identified employees who were issued shares during any one year equal to or exceeding 1% of the issued capital of the company at the time of issuance;
   (d) diluted Earning Per Share (EPS) pursuant to issuance of shares under
the scheme; and

(e) consideration received against the issuance of shares.

(ii) Check that every company that has passed a resolution for the scheme complies with the accounting policies as specified in Schedule II to the SEBI (Employee Stock Option Scheme and Employee Stock Purchase) Guidelines, 1999.

5. Preferential Allotment

Nothing in these guidelines shall apply to shares issued to employees in compliance with the Securities and Exchange Board of India Guidelines on Preferential Allotment.

6. Listing

(i) The shares arising pursuant to an ESOS and shares issued under an ESPS are required to be listed immediately upon exercise in any recognized stock exchange where the securities of the company are listed subject to compliance of the following:

(a) The ESOS/ESPS is in accordance with these Guidelines.

(b) In case of an ESOS the company has also filed with the concerned stock exchanges, before the exercise of option, a statement as per Schedule V and has obtained in-principle approval from such Stock Exchanges.

(c) As and when ESOS/ESPS are exercised the company has notified the concerned Stock Exchanges as per the statement as per Schedule VI.

(ii) (a) Ensure that the shares arising after the IPO, out of options granted under any ESOS framed prior to its IPO is being listed immediately upon exercise in all the recognized stock exchanges where the equity shares of the company are listed subject to compliance with clause 15.3 (i.e. options outstanding at IPO) and, where applicable, clause 22.2A (conditions for fresh grant of options prior to IPO).

(b) Ensure that any fresh grant of options under any ESOS framed prior to its IPO and prior to the listing of its equity shares is—

(i) in conformity with these guidelines; and

(ii) such pre-IPO scheme is ratified by its shareholders in general meeting subsequent to the IPO. However such ratification may be done any time prior to grant of new options under such pre-IPO scheme.

(c) Ensure that no change shall be made in the terms of options issued under such pre-IPO schemes, whether by repricing, change in vesting period or maturity or otherwise, unless prior approval of the shareholders is taken for such change. However, nothing in this sub-clause shall apply to any adjustments for corporate actions made in accordance with these guidelines.

(iii) For listing of shares issued pursuant to ESOS or ESPS the company is required obtain the in-principle approval from Stock Exchanges where it proposes to list the said shares.
(iv) The listed companies is required to file the ESOS or ESPS Schemes through EDIFAR filing.

(vii) When holding company issues ESOS/ESPS to the employee of its subsidiary, the cost incurred by the holding company for issuing such options/shares is required to be disclosed in the ‘notes to accounts’ of the financial statements of the subsidiary company.

In a case falling under above clause, if the subsidiary reimburses the cost incurred by the holding company in granting options to the employees of the subsidiary, both the subsidiary as well as the holding company shall disclose the payment or receipt, as the case may be, in the ‘notes to accounts’ to their financial statements.

(viii) The company shall appoint a registered Merchant Banker for the implementation of ESOS and ESPS as per these guidelines till the stage of framing the ESOS/ESPS and obtaining in-principal approval from the stock exchanges in accordance with these Guidelines.

7. ESOS/ESPS Through Trust Route

In case of ESOS/ESPS administered through a Trust, the accounts of the company shall be prepared as if the company itself is administering the ESOS/ESPS.

III-C. DUE DILIGENCE- BONUS ISSUE

Checklist for issue of Bonus shares

- Ensure that is authorised by its articles of association for issue of bonus shares, capitalisation of reserves, etc.: If there is no such provision in the articles of association, the issuer shall pass a resolution at its general body meeting making provisions in the articles of associations for capitalisation of reserve;
- Ensure that issuer has not defaulted in payment of interest or principal in respect of fixed deposits or debt securities issued by it;
- Ensure that the issuer has sufficient reason to believe that it has not defaulted in respect of the payment of statutory dues of the employees such as contribution to provident fund, gratuity and bonus;
- Ensure that the partly paid shares, if any outstanding on the date of allotment, are made fully paid up;
- It may be noted that no issuer shall make a bonus issue of equity shares if it has outstanding fully or partly convertible debt instruments at the time of making the bonus issue, unless it has made reservation of equity shares of the same class in favour of the holders of such outstanding convertible debt instruments in proportion to the convertible part thereof.
- The equity shares reserved for the holders of fully or partly convertible debt instruments shall be issued at the time of conversion of such convertible debt instruments on the same terms or same proportion on which the bonus shares were issued.
- The bonus issue shall be made out of free reserves built out of the genuine profits or securities premium collected in cash only and reserves created by revaluation of fixed assets shall not be capitalised for the purpose of issuing bonus shares.
- The bonus share shall not be issued in lieu of dividend.
• An issuer, announcing a bonus issue after the approval of its board of directors and not requiring shareholders’ approval for capitalisation of profits or reserves for making the bonus issue, shall implement the bonus issue within fifteen days from the date of approval of the issue by its board of directors. However, where the issuer is required to seek shareholders’ approval for capitalisation of profits or reserves for making the bonus issue, the bonus issue shall be implemented within two months from the date of the meeting of its board of directors wherein the decision to announce the bonus issue was taken subject to shareholders’ approval.

• Once the decision to make a bonus issue is announced, the issue can not be withdrawn.

III-D. DUE DILIGENCE - RIGHTS ISSUE

1. Record Date.
   • **Ensure that the record date has been** announced for the purpose of determining the shareholders eligible to apply for specified securities in the proposed rights issue. It may be noted that the issuer shall not withdraw rights issue after announcement of the record date.
   • If the issuer withdraws the rights issue after announcing the record date, it shall not make an application for listing of any of its specified securities on any recognised stock exchange for a period of twelve months from the record date announced. However, the issuer may seek listing of its equity shares allotted pursuant to conversion or exchange of convertible securities issued prior to the announcement of the record date, on the recognised stock exchange where its securities are listed.

2. Restriction on rights issue.

   No issuer shall make a rights issue of equity shares if it has outstanding fully or partly convertible debt instruments at the time of making rights issue, unless it has made reservation of equity shares of the same class in favour of the holders of such outstanding convertible debt instruments in proportion to the convertible part thereof.

   The equity shares reserved for the holders of fully or partially convertible debt instruments shall be issued at the time of conversion of such convertible debt instruments on the same terms on which the equity shares offered in the rights issue were issued.


   The abridged letter of offer, along with application form, shall be dispatched through registered post or speed post to all the existing shareholders at least three days before the date of opening of the issue. The letter of offer shall be given by the issuer or lead merchant banker to any existing shareholder who has made a request in this regard. The shareholders who have not received the application form may apply in writing on a plain paper, along with the requisite application money. The shareholders making application otherwise than on the application form shall not renounce their
rights and shall not utilise the application form for any purpose including renunciation even if it is received subsequently. If any shareholder makes an application on application form as well as on plain paper, the application is liable to be rejected.

4. Pricing
The issue price shall be decided before determining the record date which shall be determined in consultation with the designated stock exchange.

5. Period of subscription
A rights issue shall be open for subscription for a minimum period of fifteen days and for a maximum period of thirty days.

The issuer shall issue an advertisement for rights issue disclosing the following:
(a) the date of completion of despatch of abridged letter of offer and the application form;
(b) the centres other than registered office of the issuer where the shareholders or the persons entitled to receive the rights entitlements may obtain duplicate copies of the application forms in case they do not receive the application form within a reasonable time after opening of the rights issue;

7. Obligation of issuer/intermediaries
The obligation of issuer/intermediaries for a rights issuer, with respect to advertisement, appointment of compliance officer, redressal of investor grievances, due diligence, post issue reports, post issue advertisements etc is same as the public issue.

III-E QUALIFIED INSTITUTIONS PLACEMENT
1. Conditions for qualified institutions placement.
Ensure to satisfy the following conditions:
(a) a special resolution approving the qualified institutions placement has been passed by its shareholders;
(b) the equity shares of the same class, which are proposed to be allotted through qualified institutions placement or pursuant to conversion or exchange of eligible securities offered through qualified institutions placement, have been listed on a recognised stock exchange having nation wide trading terminal for a period of at least one year prior to the date of issuance of notice to its shareholders for convening the meeting to pass the special resolution:
However, where an issuer, being a transferee company in a scheme of merger, de-merger, amalgamation or arrangement sanctioned by a High Court under sections 391 to 394 of the Companies Act, 1956, makes qualified institutions placement, the period for which the equity shares of the same class of the transferor company were listed on a stock exchange having nation wide trading terminals shall also be considered for the purpose of computation of the period of one year.
(c) it is in compliance with the requirement of minimum public shareholding specified in the listing agreement with the stock exchange;
(d) In the special resolution, it shall be, among other relevant matters, specified that the allotment is proposed to be made through qualified institutions placement and the relevant date.

"relevant date" means:
(i) in case of allotment of equity shares, the date of the meeting in which the board of directors of the issuer or the committee of directors duly authorised by the board of directors of the issuer decides to open the proposed issue;
(ii) in case of allotment of eligible convertible securities, either the date of the meeting in which the board of directors of the issuer or the committee of directors duly authorised by the board of directors of the issuer decides to open the issue of such convertible securities or the date on which the holders of such convertible securities become entitled to apply for the equity shares.

2. Appointment of merchant banker.
A qualified institutions placement shall be managed by merchant banker(s) registered with the Board who shall exercise due diligence.

3. In-principle approval, due diligence certificate etc
The merchant banker shall, while seeking in-principle approval for listing of the eligible securities issued under qualified institutions placement, furnish to each stock exchange on which the same class of equity shares of the issuer are listed, a due diligence certificate stating that the eligible securities are being issued under qualified institutions placement and that the issuer complies with requirements under SEBI(ICDR)Regulations.

4. Placement Document:
The qualified institutions placement shall be made on the basis of a placement document which shall contain all specified material information.
The placement document shall be serially numbered and copies shall be circulated only to select investors.
The issuer shall, while seeking in-principle approval from the recognised stock exchange, furnish a copy of the placement document, a certificate confirming compliance with the provisions of this Chapter along with any other documents required by the stock exchange.
The placement document shall also be placed on the website of the concerned stock exchange and of the issuer with a disclaimer to the effect that it is in connection with a qualified institutions placement and that no offer is being made to the public or to any other category of investors.
A copy of the placement document shall be filed with the Board for its record within thirty days of the allotment of eligible securities.

5. Pricing.
The qualified institutions placement shall be made at a price not less than the average of the weekly high and low of the closing prices of the equity shares of the same class quoted on the stock exchange during the two weeks preceding the relevant date.
If eligible securities are convertible into or exchangeable with equity shares of the issuer, the issuer shall determine the price of such equity shares allotted pursuant to
such conversion or exchange taking the relevant date as decided and disclosed by it while passing the special resolution.

The issuer shall not allot partly paid up eligible securities. However, in case of allotment of non convertible debt instruments along with warrants, the allottees may pay the full consideration or part thereof payable with respect to warrants, at the time of allotment of such warrants. In case of allotment of equity shares on exercise of options attached to warrants, such equity shares shall be fully paid up.

The prices determined for qualified institutions placement shall be subject to appropriate adjustments if the issuer:
(a) makes an issue of equity shares by way of capitalization of profits or reserves, other than by way of a dividend on shares;
(b) makes a rights issue of equity shares;
(c) consolidates its outstanding equity shares into a smaller number of shares;
(d) divides its outstanding equity shares including by way of stock split;
(e) re-classifies any of its equity shares into other securities of the issuer;
(f) is involved in such other similar events or circumstances, which in the opinion of the concerned stock exchange, requires adjustments.

6. Restrictions on allotment.
- Allotment under the qualified institutions placement shall be made subject to the following conditions:
  (a) Minimum of ten per cent. of eligible securities shall be allotted to mutual funds: If the mutual funds do not subscribe to said minimum percentage or any part thereof, such minimum portion or part thereof may be allotted to other qualified institutional buyers;
  (b) No allotment shall be made, either directly or indirectly, to any qualified institutional buyer who is a promoter or any person related to promoters of the issuer: If a qualified institutional buyer who does not hold any shares in the issuer and who has acquired the said rights in the capacity of a lender shall not be deemed to be a person related to promoters.
- In a qualified institutions placement of non-convertible debt instrument along with warrants, an investor can subscribe to the combined offering of non-convertible debt instruments with warrants or to the individual securities, that is, either non-convertible debt instruments or warrants.
- The applicants in qualified institutions placement shall not withdraw their bids after the closure of the issue.

7. Minimum number of allottees.
The minimum number of allottees for each placement of eligible securities made under qualified institutions placement shall not be less than:
(a) two, where the issue size is less than or equal to two hundred and fifty crore rupees;
(b) five, where the issue size is greater than two hundred and fifty crore rupees:
Provided that no single allottee shall be allotted more than fifty per cent. of the issue size.
(2) The qualified institutional buyers belonging to the same group or who are under same control shall be deemed to be a single allottee.

**8. Validity of the special resolution.**
Allotment pursuant to the special resolution shall be completed within a period of twelve months from the date of passing of the resolution.
The issuer shall not make subsequent qualified institutions placement until expiry of six months from the date of the prior qualified institutions placement made pursuant to one or more special resolutions.

**9. Restrictions on amount raised.**
The aggregate of the proposed qualified institutions placement and all previous qualified institutions placements made by the issuer in the same financial year shall not exceed five times the net worth of the issuer as per the audited balance sheet of the previous financial year.

**10. Tenure.**
The tenure of the convertible or exchangeable eligible securities issued through qualified institutions placement shall not exceed sixty months from the date of allotment.

**11. Transferability of eligible securities.**
The eligible securities allotted under qualified institutions placement shall not be sold by the allottee for a period of one year from the date of allotment, except on a recognised stock exchange.

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**LESSON ROUND-UP**

- Public issue is mainly governed by the following legislations.
  - The Companies Act, 1956
  - Securities Contracts (Regulation) Act, 1956
  - Foreign Exchange Management Act, 1999
  - Securities Contracts Regulation (Rules) 1957
  - SEBI(ICDR) Regulation 2009
  - Listing Agreement
- Issue of stock options to employees by listed companies are governed by SEBI (ESOP &ESPS) Guidelines, 1999.
- Due diligence is carried out as part of IPO takes on added meaning and encompasses a wider scope.
- Company Secretary is a Key member of IPO team who ensures that the company has complied with pre-issue, issue, and post issue obligations.
SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation)

1. Draft a due diligence plan for the Board of Directors who are planning to launch an IPO.
2. Elaborate the check points while issuing of preferential allotments.
3. What are the pre-issue & Post issue obligations in respect of an IPO?
4. Company XYZ Limited is planning to launch an ESOP scheme and also an IPO shortly. Advise them on their drafting of ESOP scheme as a consultant of that company.
LEARNING OBJECTIVES

The objective of this study lesson is to enable the students to understand:

- Various types of debt instruments
- Regulatory Framework for issue of debt instruments
- Compliance Requirements under:
  - (a) Listing agreement (for privately placed Debentures/Debentures issued through public issue).
  - (b) SEBI (ICDR) Regulations, 2009 (Compliances with respect to convertible debt instruments)
  - (c) SEBI (Issue and Listing of Debt Securities) Regulations, 2008 (Compliance requirements with respect to non-convertible debt instruments)
  - (d) SEBI (Public Offer and Listing of Securitised Debt Instruments) Regulations, 2008

I. DEBT INSTRUMENTS AND ITS VARIOUS TYPES

A tradable form of a loan/debt is normally termed as Debt Instruments. It pertains to obligations of issuer with regards to certain future cash flows representing payment of interest and principal by the issuer to the holder (legal owner) of the instrument. There are various types of fixed income instruments, which cater to the needs of both investors and issuers. These instruments can be classified on the basis of interest, time duration, etc.

The classification instruments are given below:

**Fixed Instruments**
- Deposit (includes Time Deposit/Savings Deposit/Current Account)
- Fixed Deposit

**Interest Based Bonds**
- Coupon Bonds
- Zero Coupon Bonds

**Derived Instruments**
These instruments are not direct debt instruments. Instead they derive their value from other debt instruments.
- Mortgage Bonds
- Pass Through Certificates (PTCs)
- Participation Certificates (PCs)
**Benchmarked Instruments**

Debt instruments wherein the fixed income earned is based on some benchmark rate is called Benchmarked Instruments. For instance, the Floating Interest rate Bonds are benchmarked to either the LIBOR, MIBOR etc.

**Money Market Instruments**

- Call/Notice Money
- Treasury Bills
- Inter-Bank Term Money
- Certificate of Deposits
- Inter Corporate Deposits
- Commercial Papers
- Commercial Bills

**Hedging Instruments**

There are certain hedge instruments that help to reduce the risk of investing in Fixed income instruments.

- Interest Rate Swaps
- Interest Rate Options
- Swaptions

**Corporate Debentures**

A Debenture is a debt security issued by a company (Issuer), which offers to pay interest in lieu of the money borrowed for a certain period. In essence it represents a loan taken by the issuer who pays an agreed rate of interest during the lifetime of the instrument and repays the principal normally, unless otherwise agreed, on maturity.

Debentures are divided into different categories on the basis of:

1. Convertibility of the instrument
   - Non Convertible Debentures (NCD)
   - Partly Convertible Debentures (PCD)
   - Fully Convertible Debentures (FCD)
   - Optionally Convertible Debentures (OCD)

2. Security
   - Secured Debentures
   - Unsecured Debentures
The instruments traded can be classified into the following segments based on the characteristics of the identity of the issuer of these securities:

<table>
<thead>
<tr>
<th>Market Segment</th>
<th>Issuer</th>
<th>Instruments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Government Securities</td>
<td>Central Government</td>
<td>Zero Coupon Bonds, Coupon Bearing Bonds, Treasury Bills, STRIPS</td>
</tr>
<tr>
<td></td>
<td>State Governments</td>
<td>Coupon Bearing Bonds.</td>
</tr>
<tr>
<td>Public Sector Bonds</td>
<td>Government Agencies/Statutory Bodies</td>
<td>Govt. Guaranteed Bonds, Debentures</td>
</tr>
<tr>
<td></td>
<td>Public Sector Units</td>
<td>PSU Bonds, Debentures, Commercial Paper</td>
</tr>
<tr>
<td>Private Sector Bonds</td>
<td>Corporates</td>
<td>Debentures, Bonds, Commercial Paper, Floating Rate Bonds, Zero Coupon Bonds, Inter-Corporate Deposits</td>
</tr>
<tr>
<td></td>
<td>Banks</td>
<td>Certificates of Deposits, Debentures, Bonds</td>
</tr>
<tr>
<td></td>
<td>Financial Institutions</td>
<td>Certificates of Deposits, Bonds</td>
</tr>
</tbody>
</table>

II. RISKS ON TRADING IN DEBT SECURITIES

1. **Default Risk** is the risk that an issuer of a bond may be unable to make timely payment of interest or principal on a debt security.

2. **Interest Rate Risk** is the risk emerging from an adverse change in the interest rate prevalent in the market so as to affect the yield on the existing instruments.

3. **Reinvestment Rate Risk** is the probability of a fall in the interest rate resulting in a lack of options to invest the interest received at regular intervals at higher rates at comparable rates in the market.

4. **Counter Party Risk** refers to the failure or inability of the opposite party to the contract to deliver either the promised security or the sale-value at the time of settlement.

5. **Price Risk** refers to the possibility of not being able to receive the expected price on any order due to a adverse movement in the prices.

III. REGULATORY FRAMEWORK FOR DEBT SECURITIES

(a) Chapter X of SEBI (ICDR) Regulations, 2009
(b) Listing Agreement for Debentures issued through public issue/Rights issue.
(c) Listing agreement for privately placed Debentures
(d) SEBI (Issue and Listing of Debt Securities) Regulations, 2008
(e) SEBI (Public Offer and Listing of Securitised Debt Instruments) Regulations, 2008
(f) The Companies Act, 1956
IV. COMPLIANCE CHECK LIST
2A. SEBI (ICDR) Regulations, 2009

“specified securities” means equity shares and convertible securities;
“convertible security” means a security which is convertible into or exchangeable with equity shares of the issuer at a later date, with or without the option of the holder of the security and includes convertible debt instrument and convertible preference shares;
Thus, the conditions specified under Chapter II regarding Due Diligence – Equity shares is equally applicable to public issue of convertible debt instruments also.
Additionally, the issuer of debt instruments has to comply with the following.
In addition to other requirements laid down in these regulations, an issuer making a public issue or rights issue of convertible debt instruments shall comply with the following conditions:
(a) it has obtained credit rating from one or more credit rating agencies;
(b) it has appointed one or more debenture trustees in accordance with the provisions of section 117B of the Companies Act, 1956 and Securities and Exchange Board of India (Debenture Trustees) Regulations, 1993;
(c) it has created debenture redemption reserve in accordance with the provisions of section 117C of the Companies Act, 1956;
(d) if the issuer proposes to create a charge or security on its assets in respect of secured convertible debt instruments, it shall ensure that:
(i) such assets are sufficient to discharge the principal amount at all times;
(ii) such assets are free from any encumbrance;
(iii) where security is already created on such assets in favour of financial institutions or banks or the issue of convertible debt instruments is proposed to be secured by creation of security on a leasehold land, the consent of such financial institution, bank or lessor for a second or pari passu charge has been obtained and submitted to the debenture trustee before the opening of the issue;
(iv) the security/asset cover shall be arrived at after reduction of the liabilities having a first/prior charge, in case the convertible debt instruments are secured by a second or subsequent charge.
The issuer shall redeem the convertible debt instruments in terms of the offer document
Roll over of non convertible portion of partly convertible debt instruments.
— The non-convertible portion of partly convertible debt instruments issued by a listed issuer, the value of which exceeds fifty lakh rupees, may be rolled over without change in the interest rate, subject to compliance with the provisions of section 121 of the Companies Act, 1956 and the following conditions:
(a) seventy five per cent. of the holders of the convertible debt instruments of the issuer have, through a resolution, approved the rollover through postal ballot;
(b) the issuer has, along with the notice for passing the resolution, sent to all holders of the convertible debt instruments, an auditors’ certificate on the cash flow of the issuer and with comments on the liquidity position of the issuer;
(c) the issuer has undertaken to redeem the non-convertible portion of the partly convertible debt instruments of all the holders of the convertible debt instruments who have not agreed to the resolution;
(d) credit rating has been obtained from at least one credit rating agency registered with the Board within a period of six months prior to the due date of redemption and

2 As per supplement to study material
has been communicated to the holders of the convertible debt instruments, before the roll over;
— The creation of fresh security and execution of fresh trust deed shall not be mandatory if the existing trust deed or the security documents provide for continuance of the security till redemption of secured convertible debt instruments; Provided that whether the issuer is required to create fresh security and to execute fresh trust deed or not shall be decided by the debenture trustee.

**Conversion of optionally convertible debt instruments into equity share capital.**
— An issuer shall not convert its optionally convertible debt instruments into equity shares unless the holders of such convertible debt instruments have sent their positive consent to the issuer and non-receipt of reply to any notice sent by the issuer for this purpose shall not be construed as consent for conversion of any convertible debt instruments.
— Where the value of the convertible portion of any convertible debt instruments issued by a listed issuer exceeds fifty lakh rupees and the issuer has not determined the conversion price of such convertible debt instruments at the time of making the issue, the holders of such convertible debt instruments shall be given the option of not converting the convertible portion into equity shares;
If the upper limit on the price of such convertible debt instruments and justification thereon is determined and disclosed to the investors at the time of making the issue, it shall not be necessary to give such option to the holders of the convertible debt instruments for converting the convertible portion into equity share capital within the said upper limit.
— Where an option is to be given to the holders of the convertible debt instruments and if one or more of such holders do not exercise the option to convert the instruments into equity share capital at a price determined in the general meeting of the shareholders, the issuer shall redeem that part of the instruments within one month from the last date by which option is to be exercised, at a price which shall not be less than its face value.

**Issue of convertible debt instruments for financing**
No issuer shall issue convertible debt instruments for financing replenishment of funds or for providing loan to or for acquiring shares of any person who is part of the same group or who is under the same management: However, an issuer may issue fully convertible debt instruments for these purposes if the period of conversion of such debt instruments is less than eighteen months from the date of issue of such debt instruments.

**B. UNDER SEBI (ISSUE AND LISTING OF DEBT SECURITIES) REGULATIONS, 2008 (COMPLIANCES WITH RESPECT TO NON-CONVERTIBLE DEBT INSTRUMENTS)**

These regulations are applicable to (a) Public issue of debt securities and (b) listing of debt securities issued through public issue or on private placement basis on a recognized stock exchange.

**1. General Conditions**
— Ensure that the issuer/person in control of the issuer/promoter has not been restrained or prohibited or debarred by SEBI from accessing the securities market or dealing in securities.
— Ensure that the following conditions are satisfied as on the date of filing of draft offer document and final offer document.

— Ensure that an application is made to one or more recognized stock exchanges for listing and has chosen one of them as designated exchange and if any of such stock exchanges chosen have nationwide trading terminals, the issuer shall choose one of them as the designated stock exchange.

— Ensure that in-principal approval has been obtained for listing on the exchanges where an application has been made.

— Ensure that credit rating has been obtained from at least one credit rating agency registered with the Board and is disclosed in the offer document.

— Where credit ratings are obtained from more than one credit rating agencies, all the ratings, including the unaccepted ratings, shall be disclosed in the offer document.

— Ensure that the company has entered into an arrangement with a depository registered with the Board for dematerialization of the debt securities that are proposed to be issued to the public, in accordance with the Depositories Act, 1996 and regulations made thereunder.

2. Disclosures in the offer document

— Ensure that the offer document shall contain all material disclosures which are necessary for the subscribers of the debt securities to take an informed investment decision.

— Ensure that the offer document contains the following:

(a) the disclosures specified in Schedule II of the Companies Act, 1956;

(b) disclosure specified in Schedule I of these regulations;

(c) additional disclosures as may be specified by SEBI.

3. Filing of draft offer document

— Ensure that a draft offer document has been filed with the designated stock exchange through the lead merchant banker.

— Ensure that the draft offer document filed with the designated stock exchange has been made public by posting the same on the website of the designated stock exchange for seeking public comments for a period of seven working days from the date of filing the draft offer document with such exchange. The draft offer document may also be displayed on the website of the issuer, merchant bankers and the stock exchanges where the debt securities are proposed to be listed.

— Ensure that the draft offer document clearly specifies the names and contact particulars of the compliance officer of the lead merchant banker and the issuer including the postal and email address, telephone and fax numbers.
— Ensure that all comments received on the draft offer document are suitably addressed prior to the filing of the offer document with the Registrar of Companies.

— Ensure that a copy of draft and final offer document has been forwarded to the Board for its records, simultaneously with filing of these documents with designated stock exchange.

— Ensure that the lead merchant banker, prior to filing of the offer document with the Registrar of Companies, furnish to SEBI a due diligence certificate as per Schedule II of these regulations.

— Ensure that the debenture trustee, prior to the opening of the public issue, furnishes to SEBI a due diligence certificate as per Schedule III of these regulations.


— Ensure that the draft and final offer document is displayed on the websites of stock exchanges and shall be available for download in PDF / HTML formats.

— Ensure that the offer document is filed with the designated stock exchange, simultaneously with filing thereof with the Registrar of Companies, for dissemination on its website prior to the opening of the issue.

— Ensure that, where any person makes a request for a physical copy of the offer document, the same is being provided to him by the issuer or lead merchant banker.

5. Advertisements for Public issues

— Ensure that the issuer makes a advertisement in an national daily with wide circulation, on or before the issue opening date and such advertisement shall, amongst other things, contain the disclosures as per Schedule IV.

— Ensure that the advertisement is not misleading in material particular or which contains any information in a distorted manner or which is manipulative or deceptive.

— Ensure that the advertisement is truthful, fair and clear and does not contain a statement, promise or forecast which is untrue or misleading.

— Ensure that the advertisement does not contain any matters which are extraneous to the contents of the offer document.

— The advertisement shall urge the investors to invest only on the basis of information contained in the offer document.

— Ensure that any corporate or product advertisement issued by the issuer during the subscription period does not make any reference to the issue of debt securities or be used for solicitation.

6. Abridged Prospectus and application forms

— Ensure that:

(a) every application form issued by the issuer is accompanied by a copy of the abridged prospectus;
(b) the abridged prospectus does not contain matters which are extraneous to the contents of the prospectus;

(c) adequate space has been provided in the application form to enable the investors to fill in various details like name, address, etc.

— Ensure provide the facility for subscription of application in electronic mode.

7. Electronic Issuances

— Ensure that debt securities to the public through the on-line system of the designated stock exchange has been made in compliance with relevant applicable requirements as may be specified by the Board.

8. Price Discovery through Book Building

— The issuer may determine the price of debt securities in consultation with the lead merchant banker and the issue may be at fixed price or the price may be determined through book building process in accordance with the procedure as may be specified by the Board.

9. Minimum Subscription

— The issuer may decide the amount of minimum subscription which it seeks to raise by issue of debt securities and disclose the same in the offer document.

— Ensure that, in the event of non receipt of minimum subscription all application moneys received in the public issue has been refunded forthwith to the applicants.

10. Underwriting

— Ensure that adequate disclosures regarding underwriting arrangements if any has been disclosed in the offer document.

11. Mis-statements in the offer document.

— Ensure that the offer document does not omit disclosure of any material fact which may make the statements made therein, in light of the circumstances under which they are made, misleading.

— Ensure that the offer document or abridged prospectus or any advertisement issued by an issuer in connection with a public issue of debt securities does not contain any false or misleading statement.

12. Trust Deed

— Ensure that a trust deed for securing the issue of debt securities is executed by the issuer in favour of the debenture trustee within three months of the closure of the issue.

— Ensure that the trust deed contains such clauses as may be prescribed under section 117A of the Companies Act, 1956 and those mentioned in Schedule IV of the Securities and Exchange Board of India (Debenture Trustees) Regulations, 1993.

— Ensure that the trust deed does not contain a clause which has the effect of—
(a) limiting or extinguishing the obligations and liabilities of the debenture trustees or the issuer in relation to any rights or interests of the investors;

(b) limiting or restricting or waiving the provisions of the Act, these regulations and circulars or guidelines issued by the Board;

(c) indemnifying the debenture trustees or the issuer for loss or damage caused by their act of negligence or commission or omission.

13. Debenture Redemption Reserve

— For the redemption of the debt securities issued by a company, the issuer shall create debenture redemption reserve in accordance with the provisions of the Companies Act, 1956 and circulars issued by Central Government in this regard. It may be noted that where the issuer has defaulted in payment of interest on debt securities or redemption thereof or in creation of security as per the terms of the issue of debt securities, any distribution of dividend shall require approval of the debenture trustees.

14. Creation of security

— Ensure that the proposal to create a charge or security, if any, in respect of secured debt securities is disclosed in the offer document along with its implications.

— Ensure give an undertaking in the offer document that the assets on which charge is created are free from any encumbrances and if the assets are already charged to secure a debt, the permissions or consent to create second or pari passu charge on the assets of the issuer have been obtained from the earlier creditor.

— Ensure that issue proceeds are be kept in an escrow account until the documents for creation of security as stated in the offer document, are executed.

15. Redemption and Roll-over

— Ensure to redeem the debt securities in terms of the offer document.

— Where it is desired to roll-over the debt securities issued, ensure to pass a special resolution of holders of such securities and give twenty one days notice, containing the disclosure with regard to credit rating, rationale for roll-over etc.

— The issuer shall, prior to sending the notice to holders of debt securities, file a copy of the notice and proposed resolution with the stock exchanges where such securities are listed, for dissemination of the same to public on its website.

— The debt securities issued can be rolled over subject to the following conditions:

(a) the roll-over is approved by a special resolution passed by the holders of debt securities through postal ballot having the consent of not less than 75% of the holders by value of such debt securities;

(b) atleast one rating is obtained from a credit rating agency within a period
of six months prior to the due date of redemption and is disclosed in the notice;

(c) fresh trust deed shall be executed at the time of such roll-over or the existing trust deed may be continued if the trust deed provides for such continuation;

(d) adequate security shall be created or maintained in respect of such debt securities to be rolled-over.

— Ensure to redeem the debt securities of all the debt securities holders, who have not given their positive consent to the roll-over.

16. Listing of Debt Securities

— Ensure to make an application for listing to one or more recognized stock exchanges in terms of sub-section (1) of section 73 of the Companies Act, 1956 (1 of 1956).

— Ensure to comply with conditions of listing of such debt securities as specified in the Listing Agreement with the stock exchange where such debt securities are sought to be listed.

— An issuer may list its debt securities issued on private placement basis on a recognized stock exchange subject to the following conditions:

(a) the issuer has issued such debt securities in compliance with the provisions of the Companies Act, 1956, rules prescribed there under and other applicable laws;

(b) credit rating has been obtained in respect of such debt securities from at least one credit rating agency registered with the Board;

(c) the debt securities proposed to be listed are in dematerialized form;

(d) the disclosures as provided in regulation 21 have been made.

— The issuer shall comply with conditions of listing of such debt securities as specified in the Listing Agreement with the stock exchange where such debt securities are sought to be listed.

— The issuer making a private placement of debt securities and seeking listing thereof on a recognized stock exchange shall make disclosures as specified in Schedule I of these Securities regulations accompanied by the latest Annual Report of the issuer and such disclosures are made available on the web sites of stock exchanges where such securities are proposed to be listed and shall be available for download in PDF/HTML formats.

17. Relaxation of strict enforcement of rule 19 of Securities Contracts (Regulation) Rules, 1957 (i.e. Requirements with respect to the listing of securities on a recognised stock exchange.)

— In exercise of the powers conferred by sub-rule (7) of rule 19 of the Securities Contracts (Regulation) Rules, 1957, the Board hereby relaxes the strict enforcement of:
18. Continuous Listing

— Ensure to comply with the conditions of listing specified in the respective listing agreement for debt securities.

— Ensure that every rating obtained by an issuer is being periodically reviewed by the registered credit rating agency and any revision in the rating shall be promptly disclosed to the stock exchange(s) where the debt securities are listed.

— Ensure that any change in rating is promptly disseminated to investors and prospective investors in such manner as the stock exchange where such securities are listed may determine from time to time.

— Ensure that all information and reports on debt securities including compliance reports filed by the issuers and the debenture trustees regarding the debt securities to the investors and the general public by placing on their respective websites.

— Ensure that debenture trustees disclose the information to the investors and the general public by issuing a press release in any of the following events and the same is placed on the websites:

  (a) default by issuer to pay interest on debt securities or redemption amount;

  (b) failure to create a charge on the assets;

  (c) revision of rating assigned to the debt securities.

19. Trading of Debt securities

— The debt securities issued to the public or on a private placement basis, which are listed in recognized stock exchanges, shall be traded and such trades shall be cleared and settled in recognized stock exchanges subject to conditions specified by the Board.

— In case of trades of debt securities which have been made over the counter, such trades shall be reported on a recognized stock exchange having a nation wide trading terminal or such other platform as may be specified by the Board.

20. Obligations of Debenture Trustee

— The debenture trustee shall be vested with the requisite powers for protecting
the interest of holders of debt securities including a right to appoint a nominee director on the Board of the issuer in consultation with institutional holders of such securities.

— The debenture trustee shall carry out its duties and perform its functions under these regulations, the Securities and Exchange Board of India (Debenture Trustees) Regulations, 1993, the trust deed and offer document, with due care, diligence and loyalty.

— The debenture trustee shall ensure disclosure of all material events on an ongoing basis.

— The debenture trustees shall supervise the implementation of the conditions regarding creation of security for the debt securities and debenture redemption reserve.

21. Obligations of the Issuer, Lead Merchant Banker, etc.

— The issuer shall disclose all the material facts in the offer documents issued or distributed to the public and shall ensure that all the disclosures made in the offer document are true, fair and adequate and there is no mis-leading or untrue statements or mis-statement in the offer document.

— The Merchant Banker shall verify and confirm that the disclosures made in the offer documents are true, fair and adequate and ensure that the issuer is in compliance with these regulations as well as all transaction specific disclosures required in Schedule I of these regulations and Schedule II of the Companies Act, 1956.

— The issuer shall treat the applicants in a public issue of debt securities in a fair and equitable manner as per the procedures as may be specified by the Board.

— The intermediaries shall be responsible for the due diligence in respect of assignments undertaken by them in respect of issue, offer and distribution of securities to the public.

— No person shall employ any device, scheme or artifice to defraud in connection with issue or subscription or distribution of debt securities which are listed or proposed to be listed on a recognized stock exchange.

— The issuer and the merchant banker shall ensure that the security created to secure the debt securities is adequate to ensure 100% asset cover for the debt securities.

C. UNDER LISTING AGREEMENT FOR DEBENTURES ISSUED THROUGH PUBLIC/RIGHTS ISSUE

Important Compliance requirements

<table>
<thead>
<tr>
<th>Sl. No.</th>
<th>Particulars</th>
<th>Details</th>
<th>Clause Ref No.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Debenture trustee</td>
<td>The Company shall have a debenture trustee for each debenture issued and</td>
<td>Clause 5</td>
</tr>
<tr>
<td>Clause</td>
<td>Description</td>
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<tr>
<td>2.</td>
<td>Security&lt;br&gt;The Company shall create and maintain security ensuring adequate security cover at all times for secured debentures&lt;br&gt;Clause 7</td>
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<td></td>
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<tr>
<td>3.</td>
<td>Information to the exchange&lt;br&gt;The company shall inform about attachment, prohibitory orders, any action that results in redemption, conversion, cancellation etc of debentures, change in the Board, Auditors, change in general character of business, alteration of capital, dividend etc.&lt;br&gt;Clause 8</td>
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<tr>
<td>4.</td>
<td>Closure of books/record date&lt;br&gt;The Company shall intimate atleast 30 days before the closure of book/record date for the purpose of payment of interest/redemption as the case may be. Gap between two book closures and/or record dates would be atleast 30 days.&lt;br&gt;Clause 9</td>
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<td>5.</td>
<td>Intimation to Exchange-declaration of issue of convertible debentures&lt;br&gt;At least 7 days in advance of the date of the meetings of its Board of Directors/ Council of issuer at which the recommendation or declaration of issue of convertible debentures or of debentures carrying a right to subscribe to equity shares or any other matter affecting the interests of debenture holders is due to be considered.&lt;br&gt;Clause 10</td>
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<tr>
<td>6.</td>
<td>Intimation about issue new debentures&lt;br&gt;The Company shall intimate the Exchange in advance, of its intention to raise funds through issue of new debentures if it proposes to list such new debentures on the Exchange.&lt;br&gt;Clause 11</td>
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<tr>
<td>7.</td>
<td>Intimation about material events&lt;br&gt;Intimation to the stock exchange about material events such as strike, lock out, changes in the general character of business, disruption due to natural calamity, revision in ratings, litigation with a material impact etc.&lt;br&gt;Clause 12</td>
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<tr>
<td>8.</td>
<td>Designating company secretary or any other person as compliance&lt;br&gt;The compliance officer shall be responsible for monitoring compliance with the regulatory provisions, filing information in the EDIFAR and to designate an e-mail ID of the grievance redressal division/compliance officer&lt;br&gt;Clause 14</td>
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<td>Sl. No.</td>
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<td>Details</td>
<td>Clause Ref No.</td>
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| 9.     | Corporate Governance                 | — Boards’ composition  
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— Code of conduct  
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| 10.    | Consolidated Financial statements in case of subsidiaries | — Publication of Consolidated Financial Statements, in case of subsidiaries  
— Annual report to contain related party disclosures and other necessary disclosures  
— To furnish cash flow statement  
— Directors report to contain certain disclosures | Clause 36 |
| 11.    | Quarterly Financial Results           | — Furnishing of un-audited financial results  
— Limited review by statutory auditors  
— Intimation to stock exchange, before and after the meeting where unaudited quarterly results have been taken on record  
— Issue of press release about the above meeting etc | Clause 37 |
| 12.    | EDIFAR filing                        | Filing of information and reports on the Electronic Data Information Filing and Retrieval | Clause 38 |

**D. UNDER LISTING AGREEMENT FOR PRIVATELY PLACED DEBENTURES**

Important Compliance requirements

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<td>2.</td>
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<td>3.</td>
<td>Information to the exchange</td>
<td>The company shall inform about attachment, prohibitory orders, any action that results in redemption, conversion, cancellation etc of debentures, change in the Board, Auditors, change in general character of business, alteration of capital, dividend etc</td>
<td>Clause 8</td>
</tr>
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</table>
| 4. | Closure of books/record date | — The Company shall intimate at least 21 days before the closure of book/ record date for the purpose of payment of interest/redemption as the case may be.  
— Gap between two book closures and/or record dates would be at least 30 days. | Clause 9 |
| 5. | Intimation to Exchange-declaration of issue of convertible debentures | At least 7 days in advance of the date of the meetings of its Board of Directors/ Council of issuer at which the recommendation or declaration of issue of convertible debentures or of debentures carrying a right to subscribe to equity shares or any other matter affecting the interests of debenture holders is due to be considered. | Clause 10 |
| 6. | Intimation about issue new debentures | The Company shall intimate the Exchange in advance, of its intention to raise funds through issue of new debentures if it proposes to list such new debentures on the Exchange. | Clause 11 |
| 7. | Intimation about material events | Intimation to the stock exchange about material events such as strike, lock out, changes in the general character of business, disruption due to natural calamity, revision in ratings, litigation with a material impact etc | Clause 12 |
| 8. | Designating company | The compliance officer shall be responsible for monitoring compliance | Clause 14 |
E. UNDER SEBI (PUBLIC OFFER AND LISTING OF SECURITISED DEBT INSTRUMENTS) REGULATIONS 2008

Securitisation is the process of conversion of existing assets or future cash flows into marketable securities. In other words, securitisation deals with the conversion of assets which are not marketable into marketable ones.

Securitised Debt Instrument means any certificate or instrument by whatever name called, of the nature referred to in sub-clause (ie) of clause (h) of Section 2 of SCRA.

Section 2(h)(ie) of SCRA reads as follows:

‘Any certificate or instrument(by whatever name called), issued to an investor by any issuer being a special purpose distinct entity which possesses any debt or receivable, including mortgage debt, assigned to such entity, and acknowledging beneficial interest of such investor in such debt or receivable, including mortgage debt, as the case may be.’

Special Purpose Distinct Entity means a trust which acquires debt or receivables not out of funds mobilized by it by issuances of securitized debt instruments through one or more schemes and includes any trust set up by the National Housing Bank under National Housing Bank Act 1987 or by the National Bank for Agricultural and Rural Development Act, 1981.

The amendments in SCRA has enabled SEBI to provide for disclosure based regulation (SEBI (Public Offer And Listing Of Securitised Debt Instruments) Regulations 2008) for public issue of or listing of securitized debt instruments on the recognized stock exchanges.

These regulations are principle based and have been made taking into account the market needs, cost of the transactions, competition policy, the professional expertise of credit rating agencies, disclosures and obligations of the parties involved in the transaction.

The main features of the regulations are as follows:

(a) The special purpose distinct entity (the issuer) will be a trust and the trustees thereof will require registration from SEBI. The instrument
issued by the issuer to the investor shall acknowledge the beneficial interest of such investor in underlying debt or receivables assigned to the issuer. The issuer can undertake only the activities permitted by the regulations.

(b) The regulations permit securitization of both existing as well as future receivables.

(c) The regulations provide flexibility in terms of pay through / pass through structures.

(d) In case of public issuances listing will be mandatory. The instruments issued on private placement basis may also be listed subject to the compliance of simplified provisions of the regulations.

(e) Regulations require strict segregation of assets of each scheme.

Some Major Compliances

— Ensure that special purpose distinct entity files draft offer document with SEBI atleast 15 days before proposed opening of the issue.

— Ensure that special purpose distinct entity has made arrangements with Registered Depositories for dematerialization of the securitized debt instruments.

— Ensure that special purpose distinct entity has made an application for listing to one or more recognized exchanges in terms of 17A(2) of SCRA

— Ensure that credit rating is obtained from atleast two registered credit rating agencies and the same is disclosed in the offer document.

— Ensure that the contents of offer document has the required details and does not contain any misleading statements.

— Ensure to file necessary information/reports, post issue as directed by SEBI from time to time.

— Ensure that the special purpose distinct entity complies with its obligation relating to Minimum public offering for listing, continuous listing conditions etc.
LESSON ROUND-UP

- A tradable form of a loan/debt is normally termed as Debt Instruments.
- Debt instruments are mainly regulated by
  — SEBI (ICDR) Regulation, 2009
  — Listing Agreement for Debentures issued through public issue/Rights issue.
  — Listing agreement for privately placed Debentures
  — SEBI (Public Offer and Listing of Securitised Debt Instruments) Regulations, 2008
  — The Companies Act, 1956
- The Company shall have a debenture trustee for each debenture issued and listed by it on a exchange on a continuous basis
- The Company shall create and maintain security ensuring adequate security cover at all times for secured debentures
- Securitisation is the process of conversion of existing assets or future cash flows into marketable securities. In other words, securitisation deals with the conversion of assets which are not marketable into marketable ones.

SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation)

1. Draft a note to the Board on the various compliances under SEBI (ICDR) Regulations, 2009
2. XYZ Ltd wants to issue debenture thorough public issue and list the same in a stock exchange with nationwide terminal. Draft a compliance checklist for the Board of Directors of XYZ Ltd.
3. What are the various listing compliances under listing agreement for privately placed debentures?
4. What are the Corporate Governance requirements for a company which has listed its shares in a stock exchange through public issue?
I. CORPORATE RESTRUCTURING THROUGH MERGERS ACQUISITIONS AND TAKEOVERS – AN OVER VIEW

Introduction

Takeovers, mergers and acquisition activities continue to accelerate. From banking to oil exploration and telecommunication to power generation, companies are coming together as never before. Not only this new industries like e-commerce and biotechnology have been exploding and old industries are being transformed. Corporate Restructuring through acquisitions, mergers, amalgamations, arrangements and takeovers has become integral to corporate strategy today.

Mergers

A merger has been defined as ‘the fusion or absorption of one thing or right into another’. A merger has also been defined as an arrangement whereby the assets of two (or more) companies become vested in, or under the control of one company (which may or may not be one of the original two Companies), which has as its shareholders all or substantially all, the shareholders of the two companies.

In a merger, one of the two existing companies merges its identity into another existing company or one of more existing companies may form a new company and merge their identities into the new company by transferring their businesses and undertakings including all other assets and liabilities to the new company (hereinafter referred to as the merged company). The shareholders of the company or companies, whose identity/ies has/have been merged (hereinafter referred to as the merging company or companies, as the case may be) will have substantial shareholding in the merged company. They will be allotted shares in the merged company in exchange for the shares held by them in the merging company or companies, as the case may be, according to the shares exchange ratio incorporated in the scheme of merger as approved by all or the prescribed majority of the
shareholders of the merging company or companies and the merged company in their separate general meetings and sanctioned by the court.

CATEGORIES OF MERGERS

Mergers may be broadly classified as follows:

(i) Cogeneric — within same industries and taking place at the same level of economic activity — exploration, production or manufacturing wholesale distribution or retail distribution to the ultimate consumer.

(ii) Conglomerate – between unrelated businesses

Cogeneric Mergers

Cogeneric mergers are of two types:

*Horizontal Merger*

This class of merger is a merger between business competitors who are manufacturers or distributors of the same type of products or who render similar or same type of services for profit. It involves joining together of two or more companies which are producing essentially the same products or rendering same or similar services or their products and services directly to compete in the market with each other. Horizontal mergers result into a reduction in the number of competing companies in an industry and increase the scope for economies of scale and elimination of duplicate facilities. However, their main drawback is that they promote monopolistic trend in the industrial sector. The acquisition in 1999 of Mobil by Exxon represented a horizontal merger.

*Vertical Merger*

In a vertical merger two or more companies are complementary to each other e.g. one of the companies is engaged in the manufacture of a particular product, the other is established and expert in the marketing of that product. In this merger the two companies merge and control the production and marketing of the same product.

A vertical merger may result into smooth and efficient flow of production and distribution of a particular product and reduction in handling and stockholding costs. It also poses a risk of monopolistic trend in the industry.

Conglomerate Merger

A conglomerate merger involves coming together of two companies in different industries i.e., the businesses of the two companies are not related to each other, neither horizontally nor vertically. They lack any commonality either in their end product, or in the rendering of any specific type of service to the society. This is the type of merger of companies which are neither competitors, nor complementaries nor suppliers of a particular raw material nor consumers of a particular product or consumable. A conglomerate merger is one which is neither horizontal nor vertical. In this the merging companies operate in unrelated markets having no functional economic relationship.
Mergers may further be categorised as:

**Cash Merger**

A merger in which certain shareholders are required to accept cash for their shares while other shareholders receive shares in the continuing enterprise.

**Defacto Merger**

Defacto merger has been defined as a transaction that has the economic effect of a statutory merger but is cast in the form of an acquisition of assets.

**Down Stream Merger**

The merger of parent company into its subsidiary is called down stream merger.

**Up stream Merger**

The merger of subsidiary company into its parent company is called an up stream merger.

**Short-form Merger**

A number of statutes provide special company rules for the merger of a subsidiary into its parent where the parent owns substantially all of the shares of the subsidiary. This is known as a short form merger. Short form mergers generally may be effected by adoption of a resolution of merger by the parent company, and mailing a copy of plan of merger to all shareholders of subsidiary and filing the executed documents with the prescribed authority under the statute. This type of merger is less expensive and time consuming than the normal type of merger.

**Triangular Merger**

Triangular merger means the amalgamation of two companies by which the disappearing company is merged into subsidiary of surviving company and shareholders of the disappearing company receive shares of the surviving company.

**Reverse Merger**

Reverse merger takes place when a healthy company amalgamates with a financially weak company. In the context of the provisions of the Companies Act, 1956, there is no difference between regular merger and reverse merger. It is like any other amalgamation. [For a detailed analysis of the concept of reverse merger, refer to Gujrat High Court judgment in Bihari Mills Ltd. case (1985) 58 Comp Cas 6].

Reverse merger can be carried out through the High Court route, but where one of the merging companies is a sick industrial company under SICA, such merger must take place through BIFR. On the amalgamation becoming effective, the sick company’s name may be changed to that of the healthy company.

Reverse merger automatically makes the transferor-company entitled for the benefit of carry forward and set-off of loss and unabsorbed depreciation of the transferee-company. There is no need to comply with Section 72A of Income Tax Act.

**Amalgamation**
Amalgamation is an ‘arrangement’ or ‘reconstruction’. Amalgamation is a legal process by which two or more companies are joined together to form a new entity or one or more companies are to be absorbed or blended with another and as a consequence the amalgamating company loses its existence and its shareholders become the shareholders of new company or the amalgamated company. In case of amalgamation a new company may come into existence or an old company may survive while amalgamating company may lose its existence.

Takeover

Takeover means acquisition by one company of control over another, usually by buying all or a majority of its shares. A transaction or a series of transactions by which a person acquires control over the assets of a company is generally known as takeover of the company. On the other hand an arrangement whereby the assets of two companies vest in one is known as merger.

Regulatory Aspects

Amalgamations, mergers and takeovers are governed by the following Acts/Regulations/Rules.

1. Section 390-396 A of Companies Act, 1956
2. Companies (Court) Rules, 1959
3. Listing Agreement
4. SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997
5. Securities Contracts Regulations Act, 1957

II. TAKEOVERS

Takeover has been defined as a business transaction whereby an individual or a group of individuals or a company acquires control over the assets of a company, either directly by becoming owner of those assets or indirectly by obtaining control of the management of the company. In the ordinary case, the company taken over is smaller but in a ‘reverse takeover’ a smaller company gains control over the larger company. This is different from ‘merger’ wherein the shareholding in the combined enterprise will be spread between the shareholders of the two companies. Normally the company which wants to takeover the other company acquires the shares of the target company either in a single transaction or a series of transactions. In case of amalgamation under Section 391-394 of the Companies Act, 1956 the amalgamating as well as amalgamated company have to apply to the High Court(s) for making order of amalgamation. However, the regulatory framework for controlling the takeover activities of a company consists of the Companies Act, 1956, Listing Agreement with Stock Exchanges and SEBI’s Takeover Code.

Takeover Bid

In simple language a takeover is acquisition of shares, voting rights in a company with a view to gaining control over the management of the company.

A “takeover bid” is an offer addressed to each shareholder of a company, whose
shares are not closely held, to buy his shares in the company at the offered price within the stipulated period of time. It is addressed to the shareholders with a view to acquiring sufficient number of shares to give the offeror company, voting control of the target company. It is usually expressed to be conditional upon a specified percentage of shares being the subject-matter of acceptance by or before a stipulated date.

A takeover bid is a technique, which is adopted by a company for taking over control of the management and affairs of another company by acquiring its controlling shares.

KINDS OF TAKEOVERS

1. Friendly takeover;
2. Hostile takeover.

Friendly Takeover

A friendly takeover is with the consent of taken over company. There is an agreement between the management of two companies through negotiations and the takeover bid may be with the consent of majority or all shareholders of the target company, which is referred to as friendly takeover bid.

Hostile Takeover

When an acquirer company does not offer the target company the proposal to acquire its undertaking but silently and unilaterally pursues efforts to gain control against the wishes of existing management such acts of acquirer are known as ‘takeover raids’ or hostile ‘takeover bids’. The main distinction between a friendly takeover and hostile takeover is whether there is a mutual understanding between the acquirer and the taken over company. When there is a mutual understanding, it is friendly takeover otherwise it is termed as hostile takeover.

In a takeover, the taking over company has two options, viz., (I) to merge both companies into one and operate both the undertakings as a single entity, and (ii) to keep the takenover company a separate and independent company, with changed management, changed policies or even with a changed name.

Takeover may be of different types depending upon the intention of the management of the taking over company.

1. A takeover may be a straight takeover which is accomplished by the management of the taking over company by acquisition of shares of another company with an intention to maintain and operate the takeover company as an independent legal entity.

2. Another type of takeover may be with an intention of capturing the ownership of the takeover company in order to merge both companies into one and operate business and undertakings of both the companies as a single legal entity.

3. A third type of takeover is the takeover of a sick industrial company for the
4. Bail out takeover is substantial acquisition of shares in a financially weak company not being a sick industrial company, in pursuance to a scheme of rehabilitation approved by a public financial institution or a scheduled bank (hereinafter referred to as the lead institution). The lead institution is responsible for ensuring compliance with the provisions of the SEBI (Substantial Acquisition and Takeovers) Regulations, 1997, which regulate the bail out takeovers.

An overview of international comparison on takeovers.

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<td>Creeping acquisition limit</td>
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<td>To acquire 50% or more first and 5% over a 12 month period</td>
<td>3% in 6 months</td>
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TAKEOVER PROCESS IN INDIA – AN OVERVIEW

The following chart gives an overview of takeover process in India, when there is no competitive bid.

Conduct a Board meeting for considering public offer

Appoint Merchant Banker

Open Escrow Account

Public Announcement (PA)

File Letter of Offer (LOO) with SEBI

To carry out the modifications recommended by SEBI

To dispatch LOO to Shareholders

Opening of Offer

Payment of consideration

PA to be within 4 days of agreement with MB
PA to contain specified details and not contain misleading information.
Specified date to be mentioned in PA for the purpose of determining names of shareholders for sending LOO
Copy of PA to be filed with SEBI, Target Company and Stock Exchanges where the shares are listed

LOO to be filed with SEBI within 14 days of PA
Draft LOO to be sent to the target company also within 14 days of PA

To be dispatched not earlier than 21 days from the date of filing LOO with SEBI

Not later than 55th day of PA
Price to be made as specified in regulations
Minimum and maximum quantity offered to be taken care
Offer to be opened for at least 20 days

III. SEBI (SUBSTANTIAL ACQUISITION OF SHARES AND TAKEOVERS) REGULATIONS, 1997

(a) Important Definitions

“acquirer” means any person who, directly or indirectly, acquires or agrees to acquire shares or voting rights in the target company, or acquires or agrees to
acquire control over the target company, either by himself or with any person acting in concert with the acquirer;

“control” shall include the right to appoint majority of the directors or to control the management or policy decisions exercisable by a person or persons acting individually or in concert, directly or indirectly, including by virtue of their shareholding or management rights or shareholders agreements or voting agreements or in any other manner.

Explanation.—(i) Where there are two or more persons in control over the target company, the cesser of any one of such persons from such control shall not be deemed to be a change in control of management nor shall any change in the nature and quantum of control amongst them constitute change in control of management:

Provided that the transfer from joint control to sole control is effected in accordance with clause (e) of sub-regulation (1) of regulation 3.

(ii) If consequent upon change in control of the target company in accordance with regulation 3, the control acquired is equal to or less than the control exercised by person(s) prior to such acquisition of control, such control shall not be deemed to be a change in control;

“person acting in concert” comprises,—

(1) persons who, for a common objective or purpose of substantial acquisition of shares or voting rights or gaining control over the target company, pursuant to an agreement or understanding (formal or informal), directly or indirectly co-operate by acquiring or agreeing to acquire shares or voting rights in the target company or control over the target company,

(2) without prejudice to the generality of this definition, the following persons will be deemed to be persons acting in concert with other persons in the same category, unless the contrary is established:

(i) a company, its holding company, or subsidiary or such company or company under the same management either individually or together with each other;

(ii) a company with any of its directors, or any person entrusted with the management of the funds of the company;

(iii) directors of companies referred to in sub-clause (i) of clause (2) and their associates;

(iv) mutual fund with sponsor or trustee or asset management company;

(v) foreign institutional investors with sub-account(s);

(vi) merchant bankers with their client(s) as acquirer;

(vii) portfolio managers with their client(s) as acquirer;

(viii) venture capital funds with sponsors;

(ix) banks with financial advisers, stock brokers of the acquirer, or any company which is a holding company, subsidiary or relative of the acquirer:
Provided that sub-clause (ix) shall not apply to a bank whose sole relationship with the acquirer or with any company, which is a holding company or a subsidiary of the acquirer or with a relative of the acquirer, is by way of providing normal commercial banking services or such activities in connection with the offer such as confirming availability of funds, handling acceptances and other registration work;

(x) any investment company with any person who has an interest as director, fund manager, trustee, or as a shareholder having not less than 2 per cent of the paid-up capital of that company or with any other investment company in which such person or his associate holds not less than 2 per cent of the paid-up capital of the latter company.

Note: For the purposes of this clause “associate” means,—

(a) any relative of that person within the meaning of section 6 of the Companies Act, 1956 (1 of 1956); and

(b) family trusts and Hindu undivided families;

“promoter” means—

(a) any person who is in control of the target company;

(b) any person named as promoter in any offer document of the target company or any shareholding pattern filed by the target company with the stock exchanges pursuant to the Listing Agreement, whichever is later;

and includes any person belonging to the promoter group as mentioned in Explanation I:

Provided that a director or officer of the target company or any other person shall not be a promoter, if he is acting as such merely in his professional capacity.

Explanation I: For the purpose of this clause, “promoter group” shall include:

(a) in case promoter is a body corporate—

(i) a subsidiary or holding company of that body corporate;

(ii) any company in which the promoter holds 10 per cent or more of the equity capital or which holds 10 per cent or more of the equity capital of the promoter;

(iii) any company in which a group of individuals or companies or combinations thereof who holds 20 per cent or more of the equity capital in that company also holds 20 per cent or more of the equity capital of the target company; and

(b) in case the promoter is an individual—

(i) the spouse of that person, or any parent, brother, sister or child of that person or of his spouse;

(ii) any company in which 10 per cent or more of the share capital is held by the promoter or an immediate relative of the promoter or a firm or HUF in which the promoter or any one or more of his immediate relative is a member;

(iii) any company in which a company specified in (i) above, holds 10 per
cent or more, of the share capital; and

(iv) any HUF or firm in which the aggregate share of the promoter and his immediate relatives is equal to or more than 10 per cent of the total.

Explanation II: Financial Institutions, Scheduled Banks, Foreign Institutional Investors (FIIs) and Mutual Funds shall not be deemed to be a promoter or promoter group merely by virtue of their shareholding:

Provided that the Financial Institutions, Scheduled Banks and Foreign Institutional Investors (FIIs) shall be treated as promoters or promoter group for the subsidiaries or companies promoted by them or mutual funds sponsored by them

(b) Exemptions

SEBI (SAST) Regulations, 1997 requires the acquirer to make a public announcement and a public offer on acquisition of a certain percentage of shares or voting rights in a company. However, certain circumstances have been provided in regulation 3, subject to which if an acquirer acquires the specified percentage of shares or voting rights, he would be exempted from the requirement of making an open offer to the existing shareholders of the company which are given below.

1. Allotment in pursuance of an application made to a public issue:

Provided that if such an allotment is made pursuant to a firm allotment in the public issues, such allotment shall be exempt only if full disclosures are made in the prospectus about the identity of the acquirer who has agreed to acquire the shares, the purpose of acquisition, consequent changes in voting rights, shareholding pattern of the company and in the board of directors of the company, if any, and whether such allotment would result in change in control over the company;

2. Allotment pursuant to an application made by the shareholder for rights issue,

(i) to the extent of his entitlement; and

(ii) up to the percentage specified in regulation 11:

Provided that the limit mentioned in sub-clause (ii) will not apply to the acquisition by any person, presently in control of the company and who has in the rights letter of offer made disclosures that they intend to acquire additional shares beyond their entitlement, if the issue is undersubscribed:

Provided further that this exemption shall not be available in case the acquisition of securities results in the change of control of management;

3. Allotment to the underwriters pursuant to any underwriting agreement;

4. inter se transfer of shares amongst—

(i) group coming within the definition of group as defined in the Monopolies and Restrictive Trade Practices Act, 1969 (54 of 1969) where persons constituting such group have been shown as group in the last published Annual Report of the target company;

(ii) relatives within the meaning of section 6 of the Companies Act, 1956 (1 of 1956);
(iii) (a) Qualifying Indian promoters and foreign collaborators who are shareholders;

(b) Qualifying promoters:

Provided that the transferor(s) as well as the transferee(s) have been holding shares in the target company for a period of at least three years prior to the proposed acquisition.

Explanation: For the purpose of the exemption under sub-clause (iii) the term “qualifying promoter” means—

(i) any person who is directly or indirectly in control of the company; or

(ii) any person named as promoter in any document for offer of securities to the public or existing shareholders or in the shareholding pattern disclosed by the company under the provisions of the Listing Agreement, whichever is later;

and includes,

(a) where the qualifying promoter is an individual,—

(1) a relative of the qualifying promoter within the meaning of section 6 of the Companies Act, 1956 (1 of 1956);

(2) any firm or company, directly or indirectly, controlled by the qualifying promoter or a relative of the qualifying promoter or a firm or Hindu undivided family in which the qualifying promoter or his relative is a partner or a coparcener or a combination thereof:

Provided that, in case of a partnership firm, the share of the qualifying promoter or his relative, as the case may be, in such firm should not be less than fifty per cent (50%);

(b) where the qualifying promoter is a body corporate,—

(1) a subsidiary or holding company of that body; or

(2) any firm or company, directly or indirectly, controlled by the qualifying promoter of that body corporate or by his relative or a firm or Hindu undivided family in which the qualifying promoter or his relative is a partner or coparcener or a combination thereof:

Provided that, in case of a partnership firm, the share of such qualifying promoter or his relative, as the case may be, in such firm should not be less than fifty per cent (50%);

(iv) the acquirer and persons acting in concert with him, where such transfer of shares takes place three years after the date of closure of the public offer made by them under these regulations.

Explanation.—(1) The exemption under sub-clauses (iii) and (iv) shall not be available if inter se transfer of shares is at a price exceeding 25% of the price as determined in terms of sub-regulations (4) and (5) of regulation 20.

(2) The benefit of availing exemption under this clause, from applicability of the regulations for increasing shareholding or inter se transfer of shareholding shall be subject to such transferor(s) and transfereee(s) having complied with regulation 6, regulation 7 and regulation 8;
5. acquisition of shares in the ordinary course of business by,—
   (i) a registered stock-broker of a stock exchange on behalf of clients;
   (ii) a registered market maker of a stock exchange in respect of shares for which he is the market maker, during the course of market making;
   (iii) by Public Financial Institutions on their own account;
   (iv) by banks and public financial institutions as pledgees;
   (v) the International Finance Corporation, Asian Development Bank, International Bank for Reconstruction and Development, Commonwealth Development Corporation and such other international financial institutions;
   (vi) a merchant banker or a promoter of the target company pursuant to a scheme of safety net under the provisions of the Securities and Exchange Board of India (Disclosure and Investor Protection) Guidelines, 2000 in excess of limit specified in sub-regulation (1) of regulation 11;
6. Acquisition of shares by a person in exchange of shares received under a public offer made under these regulations;
7. Acquisition of shares by way of transmission on succession or inheritance;
8. Acquisition of shares by Government companies within the meaning of section 617 of the Companies Act, 1956 (1 of 1956), and statutory corporations:
   Provided that this exemption shall not be applicable if a Government company acquires shares or voting rights or control of a listed Public Sector Undertaking through the competitive bidding process of the Central Government or the State Government as the case may be, for the purpose of disinvestment;
9. Transfer of shares from State level financial institutions, including their subsidiaries, to co-promoter(s) of the company (or their successors or assignee(s) or an acquirer who has substituted an erstwhile promoter) pursuant to an agreement between such financial institution and such co-promoter(s);
10. Transfer of shares from venture capital funds or foreign venture capital investors registered with the Board to promoters of a venture capital undertaking or venture capital undertaking pursuant to an agreement between such venture capital fund or foreign venture capital investors with such promoters or venture capital undertaking;
11. Pursuant to a scheme:
   (i) framed under section 18 of the Sick Industrial Companies (Special Provisions) Act, 1985 (1 of 1986);
   (ii) of arrangement or reconstruction including amalgamation or merger or demerger under any law or regulation, Indian or foreign;
12. Change in control by takeover of management of the borrower target company by the secured creditor or by restoration of management to the said target company by the said secured creditor in terms of the Securitization
and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (54 of 2002);

13. Acquisition of shares in companies whose shares are not listed on any stock exchange. However, the said exemption shall not be applicable if by virtue of acquisition or change of control of any unlisted company, whether in India or abroad, the acquirer acquires shares or voting rights or control over a listed company;

14. Acquisition of shares in terms of guidelines or regulations regarding delisting of securities specified or framed by the Board;

15. Other cases as may be exempted under regulation 4 (i.e on application to Takeover panel).

It may be noted that nothing contained in point no 1-15 shall affect the applicability of the listing requirements.

16. Acquisition of Global Depository Receipts or American Depository Receipts as long as they are not converted into shares carrying voting rights.

(c) Disclosures

(i) Initial/periodic Disclosures (Regulation 7)

Acquirer

(1) Any acquirer, who acquires shares or voting rights which (taken together with shares or voting rights, if any, held by him) would entitle him to more than five per cent or ten per cent or fourteen per cent or fifty four per cent or seventy four per cent shares or voting rights in a company, in any manner whatsoever, shall disclose at every stage the aggregate of his shareholding or voting rights in that company to the company and to the stock exchanges where shares of the target company are listed.

(2) Any acquirer whose existing holding is between 15% to 55% of the shares or voting rights in a company (as referred in regulation (11(1)), shall disclose purchase or sale aggregating two per cent or more of the share capital of the target company to the target company, and the stock exchanges where shares of the target company are listed within two days of such purchase or sale along with the aggregate shareholding after such acquisition or sale.

In respect of point no 1 and 2 the term ‘acquirer’ shall include a pledgee, other than a bank or a financial institution and such pledgee shall make disclosure to the target company and the stock exchange within two days of creation of pledge.

(3) The disclosures mentioned in point no 1 and 2 shall be made within two days of,—

(a) the receipt of intimation of allotment of shares; or

(b) the acquisition of shares or voting rights, as the case may be.

Company

Every company, has received initial disclosure from an acquirer, shall disclose to all the stock exchanges on which the shares of the said company are listed the aggregate number of shares held by each of such persons referred above within seven days of receipt of information from acquirer.
(ii) Continual disclosures. (Regulation 8)

Acquirer/Promoter

(1) Every person, including a person mentioned in regulation 6 (ie transitional provisions relating to shares acquired before SEBI (SAST) Regulations, 1997 came into force) who holds more than fifteen per cent shares or voting rights in any company, shall, within 21 days from the financial year ending March 31, make yearly disclosures to the company, in respect of his holdings as on 31st March.

(2) A promoter or every person having control over a company shall, within 21 days from the financial year ending March 31, as well as the record date of the company for the purposes of declaration of dividend, disclose the number and percentage of shares or voting rights held by him and by persons acting in concert with him, in that company to the company.

Company

Every company whose shares are listed on a stock exchange, shall within 30 days from the financial year ending March 31, as well as the record date of the company for the purposes of declaration of dividend, make yearly disclosures to all the stock exchanges on which the shares of the company are listed, the changes, if any, in respect of acquirer/promoter (ie the holdings of the persons referred to under sub-regulation (1) of SEBI(SAST) Regulations, 1997) and also holdings of promoters or person(s) having control over the company as on 31st March.

Disclosure of pledged shares

8A. (1) A promoter or every person forming part of the promoter group of any company is required to disclose details of shares of that company pledged by him, if any, to that company, within 7 working days from the date of creation of pledge on shares of that company held by him, inform the details of such pledge of shares to that company.

A promoter or every person forming part of the promoter group of any company shall, within 7 working days from the date of invocation of pledge on shares of that company pledged by him, inform the details of invocation of such pledge to that company.

The company shall disclose the information received as above to all the stock exchanges, on which the shares of company are listed, within 7 working days of the receipt thereof, if, during any quarter ending March, June, September and December of any year,:-

(a) aggregate number of pledged shares of a promoter or every person forming part of promoter group taken together with shares already pledged during that quarter by such promoter or persons exceeds twenty five thousand; or

(b) aggregate of total pledged shares of the promoter or every person forming part of promoter group alongwith the shares already pledged during that quarter by such promoter or persons exceeds one per cent. of total shareholding or voting rights of the company, whichever is lower.”

(d) Trigger points

Trigger point is a point where provisions of SEBI (SAST) Regulations, 1997 i.e takeover code gets triggered and the acquirer is required to follow public announcement and other requirements as mentioned in the regulations in respect of
further acquisition. Following are the trigger points where an acquirer is required to follow SEBI(SAST) Regulations, 1997.

(i) **15% shares or voting rights:**

An acquirer together with persons acting in concert who intends to acquire shares which along with his existing shareholding would entitle him to exercise 15% or more voting rights, can acquire such additional shares only after making a public announcement (PA) to acquire at least additional 20% of the voting capital of Target Company from the shareholders through an open offer.

(ii) **Creeping acquisition limit:**

An acquirer together with persons acting in concert who holds 15% or more but less than 55% of shares or voting rights of a target company, can acquire such additional shares as would entitle him to exercise more than 5% of the voting rights in any financial year ending March 31 only after making a public announcement to acquire at least additional 20% shares of target company from the shareholders through an open offer.

(iii) **Consolidation of holding:**

An acquirer who holds 55% or more but less than 75% shares or voting rights of a target company, can acquire additional shares or voting rights only after making a public announcement to acquire at least additional 20% shares of target company from the shareholders through an open offer.

(e) **Public Announcement**

A public announcement is an announcement made by the acquirer through a merchant banker, primarily disclosing his intention to acquire shares of the target company from existing shareholders by means of an open offer. This is to ensure that the shareholders of the target company are aware of an exit opportunity available to them.

The disclosures in the announcement include the identity of acquirer, purpose of acquisition, offer price, number of shares to be acquired from the public, future plans of acquirer regarding the target company, change in control over the target company, if any, the procedure to be followed by acquirer in accepting the shares tendered by the shareholders and the time slap for completing all the formalities.

**Relaxation from the strict compliance of provisions of Chapter III in certain cases.**

As per Regulation 29A, the SEBI may, on an application made by a target company, relax any or more of the provisions of this Chapter, subject to such conditions as it may deem fit, if it is satisfied that –

(a) the Central Government or State Government or any other regulatory authority has removed the board of directors of the target company and has appointed other persons to hold office as directors thereof under any law for the time being in force for orderly conduct of the affairs of the target company;

(b) such directors have devised a plan which provides for transparent, open, and
competitive process for continued operation of the target company in the
interests of all stakeholders in the target company and such plan does not
further the interests of any particular acquirer;

(c) the conditions and requirements of the competitive process are reasonable
and fair;

(d) the process provides for details including the time when the public offer
would be made, completed and the manner in which the change in control
would be effected;

(e) the provisions of this Chapter are likely to act as impediment to
implementation of the plan of the target company and relaxation from one or
more of such provisions is in public interest, the interest of investors and the
securities market."

It may be noted, under Regulation 25 no competitive bid shall be made on public
announcement made under Regulation 29A.

For detailed provisions students are advised to refer chapter IV of ‘Corporate
Restructuring and Insolvency’

IV. CHECKLISTS ON TAKEOVERS

A. Checklist for Acquirer

1. Preliminary Examination of a target company:

   The acquirer has to undertake a preliminary study on the target company, before
taking any action for taking over a company. He may consider the following points.

   It may be noted that this list is not an exhaustive checklist and it varies depends
on size of the company nature of industry

   (a) Information has to be collected on Target Company and to be analysed on
financial and legal angle.
   (b) Register of members to be examined to verify the profile of the shareholders.
   (c) Title of the target company with respect to immovable properties may be
verified.
   (d) Financial statements of Target Company have to be examined.
   (e) Examination of Articles and Memorandum of Association of the Company.
   (f) Examination of charges created by the Company
   (g) Applicability of FEMA provisions if any relating to FDI has to be looked into.
   (h) Import and Export of technology if any
   (i) Business prospects etc.

   List/details of documents to be obtained from target company is enclosed as
Annexure A.

2. Board Meeting has to be convened to consider and decide about takeover.

3. Necessary Resolution has to be passed at the General Meeting and the
relevant forms are to be filed with Registrar of Companies.
4. **A merchant Banker of Category I have to be appointed.** It has to be ensured that the merchant banker is not an associate of or group of acquirer or the target company.

5. **Escrow Account:**

   (i) An escrow account has to be opened and the following sum has to be deposited.

   (ii) The escrow amount shall be calculated in the following manner, as specified in the sub-regulation 2 of regulation 28,—

   (a) For consideration payable under the public offer,—

   up to and including Rs. 100 crores 25 per cent;
   exceeding Rs. 100 crores 25 per cent;
   up to Rs. 100 crores and 10 per cent thereafter.

   (b) For offers which are subject to a minimum level of acceptance, and the acquirer does not want to acquire a minimum of 20 per cent, than 50 per cent of the consideration payable under the public offer in cash shall be deposited in the escrow account.

   (iii) The escrow account referred to in sub-regulation (1) shall consist of,—

   (a) cash deposited with a scheduled commercial bank; or
   (b) bank guarantee in favour of the merchant banker; or
   (c) deposit of acceptable securities with appropriate margin, with the merchant banker; or
   (d) cash deposited with a scheduled commercial bank in case of clause (b) of sub-regulation (2) of regulation 28, as mentioned in the abovesaid paragraphs.

   (iv) In case the escrow account consists of deposit with a scheduled commercial bank, the acquirer has to ensure while opening the account that the merchant banker appointed for the offer is empowered to instruct the bank to issue a banker’s cheque or demand draft for the amount lying to the credit of the escrow account, as provided in the regulations.

   (v) If the escrow account consists of bank guarantee, such bank guarantee must be in favour of the merchant banker and shall be valid at least for a period commencing from the date of public announcement until twenty days after the closure of the offer.

   (vi) In case there is any upward revision of offer, consequent upon a competitive bid or otherwise, the value of the escrow account must be increased to equal at least 10 per cent of the consideration payable upon such revision.

6. **Undertakings/Authorisation:**

   Ensure to obtain following undertakings/authorization.

   1. A letter duly authorizing Target Company to realize the value of escrow account in terms of Takeover Regulations.

   2. An undertaking to Target Company that none of the Acquirer/Persons Acting in Concert have been prohibited by SEBI from dealing in securities, in terms
of direction issued under Section 11B of SEBI Act.

3. An undertaking from the sellers, promoters, directors of the Target Company that they have not been prohibited by SEBI from dealing in securities, in terms of direction issued under Section 11B of SEBI Act.

4. An undertaking from the Target Company that it has complied with the provisions of Listing Agreement, and that any non-compliance or delayed compliance has been brought to the notice of Target Company.

5. An undertaking from the Target Company that it has complied with the provisions of SEBI (SAST) Regulations, and that any non-compliance or delayed compliance has been brought to the notice of Target Company.

7. **Public announcement (PA):**

   Before making public announcement it has to be ensured that the acquirer is able to implement the offer.

   (i) **When to make**

   (a) PA has to be made within 4 days of entering into an agreement for acquisition of shares or voting rights.

   (b) In case of disinvestment of a Public Sector Undertaking, the public announcement shall be made by the merchant banker not later than 4 working days of the acquirer executing the Share Purchase Agreement or Shareholders Agreement with the Central Government or the State Government as the case may be, for the acquisition of shares or voting rights exceeding the percentage of shareholding referred to in regulation 10 or regulation 11 or the transfer of control over a target Public Sector Undertaking.

   (c) In the case of an acquirer acquiring securities, including Global Depository Receipts or American Depository Receipts which, when taken together with the voting rights, if any already held by him or persons acting in concert with him, would entitle him to voting rights, exceeding the percentage specified in regulation 10 or regulation 11, the public announcement referred to in sub-regulation (1) shall be made not later than four working days before he acquires voting rights on such securities upon conversion, or exercise of option, as the case may be.

   (d) The public announcement referred to in regulation 12 (ie Acquisition of control over a company) shall be made by the merchant banker not later than four working days after any such change or changes are decided to be made as would result in the acquisition of control over the target company by the acquirer.

   (e) In case of indirect acquisition or change in control, a public announcement shall be made by the acquirer within three months of consummation of such acquisition or change in control or restructuring of the parent or the company holding shares of or control over the target company in India.

   (ii) **Where to make**

   PA has to be made in all editions of one English national daily with wide circulation, one Hindi national daily with wide circulation and a regional language
daily with wide circulation at the place where the registered office of the target company is situated and at the place of the stock exchange where the shares of the target company are most frequently traded.

(iii) **What to make**

The public announcement has to contain the following particulars:

(i) the paid-up share capital of the target company, the number of fully paid-up and partly paid-up shares;

(ii) the total number and percentage of shares proposed to be acquired from the public, subject to a minimum as specified in sub-regulation (1) of regulation 21;

(iii) the minimum offer price for each fully paid-up or partly paid-up share;

(iv) mode of payment of consideration;

(v) the identity of the acquirer(s) and in case the acquirer is a company or companies, the identity of the promoters and, or the persons having control over such company(ies) and the group, if any, to which the company(ies) belong;

(vi) the existing holding, if any, of the acquirer in the shares of the target company, including holdings of persons acting in concert with him;

(via) the existing shareholding, if any, of the merchant banker in the target company;

(vii) the salient features of the agreement, if any, such as the date, the name of the seller, the price at which the shares are being acquired, the manner of payment of the consideration and the number and percentage of shares in respect of which the acquirer has entered into the agreement to acquire the shares or the consideration, monetary or otherwise, for the acquisition of control over the target company, as the case may be;

(viii) the highest and the average price paid by the acquirer or persons acting in concert with him for acquisition, if any, of shares of the target company made by him during the twelve months period prior to the date of public announcement;

(ix) the object and purpose of the acquisition of the shares and future plans, if any, of the acquirer for the target company, including disclosures whether the acquirer proposes to dispose of or otherwise encumber any assets of the target company in the succeeding two years except in the ordinary course of business of the target company:

Provided that where the future plans are set out, the public announcement shall also set out how the acquirers propose to implement such future plans:

Provided further that the acquirer shall not sell, dispose of or otherwise encumber any substantial asset of the target company except with the prior approval of the shareholders;

(ix-a) an undertaking that the acquirer shall not sell, dispose of or otherwise encumber any substantial asset of the target company except with the prior approval of the shareholders
(x) the “specified date” as mentioned in regulation 19;
(xi) the date by which individual letters of offer would be posted to each of the shareholders;
(xii) the date of opening and closure of the offer and the manner in which and the date by which the acceptance or rejection of the offer would be communicated to the shareholders;
(xiii) the date by which the payment of consideration would be made for the shares in respect of which the offer has been accepted;
(xiv) disclosure to the effect that firm arrangement for financial resources required to implement the offer is already in place, including details regarding the sources of the funds whether domestic, i.e., from banks, financial institutions or otherwise or foreign, i.e., from Non-Resident Indians or otherwise;
(xv) provision for acceptance of the offer by person(s) who own the shares but are not the registered holders of such shares;
(xvi) statutory approvals, if any, required to be obtained for the purpose of acquiring the shares under the Companies Act, 1956 (1 of 1956), the Monopolies and Restrictive Trade Practices Act, 1969 (54 of 1969), the Foreign Exchange Regulation Act, 1973 (46 of 1973), and/or any other applicable laws;
(xvii) approvals of banks or financial institutions required, if any;
(xviii) whether the offer is subject to a minimum level of acceptances from the shareholders; and
(xix) such other information as is essential for the shareholders to make an informed decision in regard to the offer.

(iv) To whom copy of Public Announcement to be submitted

Simultaneously with publication of the public announcement in the newspaper, a copy of the public announcement shall be,

(i) submitted to the Board through the merchant banker,

(ii) sent to all the stock exchanges on which the shares of the company are listed for being notified on the notice board,

(iii) sent to the target company at its registered office for being placed before the Board of Directors of the company

(v) Other aspects on public announcement

(a) It has to be ensured that the public announcement of the offer or any other advertisement, circular, brochure, publicity material or letter of offer issued in relation to the acquisition of shares is not containing any misleading information.

(b) The public announcement has to specify a date, which shall be the “specified date” for the purpose of determining the names of the shareholders to whom the letter of offer should be sent and it has to be ensured that such specified date shall not be later than the thirtieth day from the date of the public
8. Letter of Offer:

(a) Within fourteen days from the date of public announcement made under regulation 10, 11 or 12 as the case may be, the acquirer shall, through its merchant banker, file with the Board, the draft of the letter of offer containing disclosures as specified by the Board along with requisite fee.

(b) It has to be ensured to dispatch Letter of Offer to shareholders not earlier than 21 days from its submission to SEBI.

(c) Changes or modification if any given by SEBI within 21 days of filing the draft letter of offer has to be incorporated before its dispatch to the shareholders.

(d) It has to be ensured that the letter of offer would reach the shareholders on specified date within 45 days of public announcement.

(e) A copy of letter of offer shall also be sent to custodians of ADRs/GDRs/ Holders of convertible debentures, when the conversion falls within offer period.

9. Offer Price:

(i) It has to be ensured that the offer price shall be the highest of—

(a) the negotiated price under the agreement (referred to in sub-regulation (1) of regulation 14);

(b) price paid by the acquirer or persons acting in concert with him for acquisition, if any, including by way of allotment in a public or rights or preferential issue during the twenty-six week period prior to the date of public announcement, whichever is higher;

(c) the average of the weekly high and low of the closing prices of the shares of the target company as quoted on the stock exchange where the shares of the company are most frequently traded during the twenty-six weeks or the average of the daily high and low of the prices of the shares as quoted on the stock exchange where the shares of the company are most frequently traded during the two weeks preceding the date of public announcement, whichever is higher:

However, the requirement of average of the daily high and low of the closing prices of the shares as quoted on the stock exchange where the shares of the company are most frequently traded during the two weeks preceding the date of public announcement shall not be applicable in case of disinvestment of a Public Sector Undertaking.

(ii) In case of disinvestment of a Public Sector Undertaking, the relevant date for the calculation of the average of the weekly prices of the shares of the Public Sector Undertaking, as quoted on the stock exchange where its shares are most frequently traded, shall be the date preceding the date when the Central Government or the State Government opens the financial bid.

(iii) If the shares of the target company are infrequently traded, the offer price shall be determined by the acquirer and the merchant banker taking into account the following factors:
(a) the negotiated price under the agreement (referred to in sub-regulation (1) of regulation 14);

(b) the highest price paid by the acquirer or persons acting in concert with him for acquisitions, if any, including by way of allotment in a public or rights or preferential issue during the twenty-six week period prior to the date of public announcement;

(c) other parameters including return on networth, book value of the shares of the target company, earning per share, price earning multiple vis-a-vis the industry average:

If necessary, the Board may require valuation of such infrequently traded shares by an independent merchant banker (other than the manager to the offer) or an independent chartered accountant of minimum ten years’ standing or a public financial institution.

For the purpose of above, shares shall be deemed to be infrequently traded if on the stock exchange, the annualised trading turnover in that share during the preceding six calendar months prior to the month in which the public announcement is made is less than five per cent (by number of shares) of the listed shares. For this purpose, the weighted average number of shares listed during the said six months period may be taken.

(iv) In case of disinvestment of a Public Sector Undertaking, the shares of such an undertaking shall be deemed to be infrequently traded, if on the stock exchange, the annualised trading turnover in the shares during the preceding six calendar months prior to the month, in which the Central Government or the State Government as the case may be opens the financial bid, is less than five per cent (by the number of shares) of the listed shares. For this purpose, the weighted average number of shares listed during the six months period may be taken.

(v) In case of shares which have been listed within six months preceding the public announcement, the trading turnover may be annualised with reference to the actual number of days for which the shares have been listed.

(vi) In case of disinvestment of a Public Sector Undertaking, whose shares are infrequently traded, the minimum offer price shall be the price paid by the successful bidder to the Central Government or the State Government, arrived at after the process of competitive bidding of the Central Government or the State Government for the purpose of disinvestment.

(vii) If the acquirer has acquired shares in the open market or through negotiation or otherwise, after the date of public announcement at a price higher than the offer price stated in the letter of offer, then, the highest price paid for such acquisition shall be payable for all acceptances received under the offer:

However, no such acquisition shall be made by the acquirer during the last seven working days prior to the closure of the offer:

(viii) The offer price for indirect acquisition or control shall be determined with reference to the date of the public announcement for the parent company and the date of the public announcement for acquisition of shares of the
target company, whichever is higher, in accordance with sub-regulation (4) or sub-regulation (5).

(ix) It has to be ensured that all other conditions in regulation 20 regarding offer price is fulfilled.

10. Minimum voting capital:

It has to be ensured that minimum of 20% of voting capital of the company is being offered subject to minimum public holding requirements.

11. Date of opening of offer:

The date of opening of offer has to be not later than the 55th day from the date of public announcement.

12. Period of offer:

The offer to acquire should remain open for a period of minimum twenty days.

13. Competitive Bid and Revision:

Ensure to revise the offer price in consultation with merchant bankers in case of competitive bid if any.

14. Consideration-cash:

For the amount of consideration payable in cash, the acquirer shall, within a period of seven days from the date of closure of the offer, open a special account with a banker to an issue registered with the Board and deposit therein, such sum as would, together with 90 per cent of the amount lying in the escrow account, if any, make up the entire sum due and payable to the shareholders as consideration for acceptances received and accepted in terms of these regulations and for this purpose, transfer the funds from the escrow account.

15. Consideration-Securities:

In respect of consideration payable by way of exchange of securities, the acquirer shall ensure that the securities are actually issued and despatched to the shareholders.

B. Checklist for Target Company

1. Restriction on transfer or disposal of assets during offer period

The board of directors of the target company shall not, during the offer period,—

(a) sell, transfer, encumber or otherwise dispose of or enter into an agreement for sale, transfer, encumbrance or for disposal of assets otherwise, not being sale or disposal of assets in the ordinary course of business, of the company or its subsidiaries; or

(b) issue or allot any authorised but unissued securities carrying voting rights during the offer period; or

(c) enter into any material contracts,
unless the approval of the general body of shareholders is obtained after the date of the public announcement of offer

Restriction on issue of securities under point 1(b) shall not affect—

(i) the right of the target company to issue or allot shares carrying voting rights upon conversion of debentures already issued or upon exercise of option against warrants, as per pre-determined terms of conversion or exercise of option;

(ii) issue or allotment of shares pursuant to public or rights issue in respect of which the offer document has already been filed with the Registrar of Companies or Stock Exchanges, as the case may be.

2. Furnishing of information to acquirer

The target company shall furnish to the acquirer, within seven days of the request of the acquirer or within seven days from the specified date whichever is later, a list of shareholders or warrant holders or convertible debenture holders as are eligible for participation.

3. Other restrictions

Once the public announcement has been made, the board of directors of the target company shall not,—

(a) appoint as additional director or fill in any casual vacancy on the board of directors, by any person(s) representing or having interest in the acquirer, till the date of certification by the merchant banker on fulfillment of obligations by acquirer.

However, upon closure of the offer and the full amount of consideration payable to the shareholders being deposited in the special account, changes as would give the acquirer representation on the board on control over the company can be made by the target company;

(b) allow any person or persons representing or having interest in the acquirer, if he is already a director on the board of the target company before the date of the public announcement, to participate in any matter relating to the offer, including any preparatory steps leading thereto.

4. Unbiased recommendations to shareholder on open offer

The board of directors of the target company may, if they so desire, send their unbiased comments and recommendations on the offer(s) to the shareholders, keeping in mind the fiduciary responsibility of the directors to the shareholders and for the purpose seek the opinion of an independent merchant banker or a committee of independent directors:

In may be noted that for any mis-statement or for concealment of material information, the directors shall be liable for action in terms of these regulations and the Act.

5. Facilitation for verification of securities
The board of directors of the target company shall facilitate the acquirer in verification of securities tendered for acceptances.

6. Transfer of Securities

Upon fulfillment of all obligations by the acquirers under the regulations as certified by the merchant banker, the board of directors of the target company shall transfer the securities acquired by the acquirer, whether under the agreement or from open market purchases, in the name of the acquirer and/or allow such changes in the board of directors as would give the acquirer representation on the board or control over the company.

7. Post Acquisition Measures

The issues of cultural integration and the issues of human behavior need to be addressed. For the purpose, following checks have to be made constantly to ensure that:

— sensitive areas of the company are pinpointed and personnel in these sections carefully monitored;

— serious efforts are made to retain key people;

— a replacement policy is ready to cope with inevitable personnel loss;

— records are kept of everyone who leaves, when, why and to where;

— employees are informed of what is going on, even bad news is systematically delivered. Uncertainty is more dangerous than the clear, logical presentation of unpleasant facts;

— training department is fully geared to provide short, medium and long term training strategy for both production and managerial staff;

— likely union reaction be assessed in advance;

— estimate cost of redundancy payments, early pensions and the like assets;

— comprehensive policies and procedures be maintained up for employee related issues such as office procedures, new reporting, compensation, recruitment and selection, performance, termination, disciplinary action etc.;

— new policies to be clearly communicated to the employees specially employees at the level of managers, supervisors and line manager to be briefed about the new responsibilities of those reporting to them;

— family gatherings and picnics be organised for the employees and their families of merging companies during the transition period to allow them to get off their inhibitions and breed familiarity.

C. Checklist for Merchant Banker

1. Before the public announcement of offer is made, the merchant banker is required to ensure that—

   (a) the acquirer is able to implement the offer;

   (b) the provision relating to escrow account referred to in regulation 28 has been made;
(c) firm arrangements for funds and money for payment through verifiable means to fulfil the obligations under the offer are in place;

(d) the public announcement of offer is made in terms of the regulations;

(e) his shareholding, if any in the target company is disclosed in the public announcement and the letter of offer.

To ensure the above said points and for the purpose of carrying out a proper due diligence, it is advisable to obtain certain information from the acquirer and target company, which is given as Annexure B.

2. **Due diligence certificate**: The merchant banker must furnish to the Board a due diligence certificate which shall accompany the draft letter of offer.

3. The merchant banker shall ensure that the public announcement and the letter of offer is filed with the Board, target company and also sent to all the stock exchanges on which the shares of the target company are listed in accordance with the regulations.

4. The merchant banker shall ensure that the contents of the public announcement of offer as well as the letter of offer are true, fair and adequate and based on reliable sources, quoting the source wherever necessary.

5. The merchant banker shall ensure compliance of the regulations and any other laws or rules as may be applicable in this regard.

6. The merchant banker shall not deal in the shares of the target company during the period commencing from the date of his appointment in terms of regulation 13 till the expiry of the fifteen days from the date of closure of the offer.

7. Upon fulfilment of all obligations by the acquirers under the regulations, the merchant banker shall cause the bank with whom the escrow amount has been deposited to release the balance amount to the acquirers.

8. The merchant banker shall send a final report to the Board within 45 days from the date of closure of the offer.

**V. CULTURAL ISSUES ON MERGERS, ACQUISITIONS AND TAKE OVERS**

Accenture and the Economist Intelligence Unit in the first half of 2006, surveyed senior executives in North America, Europe and Asia on their mergers and acquisitions (M&A) activities and their experience in integrating companies. Similar survey was also administered to 156 executives based in India during the fourth quarter of 2006.

Of the total respondents in India, 40% were senior-level. About 64% were from companies that had global annual revenues of US$100m or more and 36% had revenues of US$1bn or more. 45% executive mainly played roles in strategy and business development and 42% in general management. Their companies were from a wide range of industries, including financial services (25%), IT and technology (21%) and professional services (13%).

Following are the key findings of the survey on human and cultural factors.
Human and Cultural Factors

Accenture Survey points out that for integrating a cross border company, 43%, respondents found addressing cultural issues as critical. The real challenge, after an acquisition is, therefore, the integration of the two companies. That is why the integration should be given a focused attention. There should be a focus on aligning the acquired company's processes through the business excellence model.

Human Factor

Studies on post-acquisition performance have primarily been a centre of interest of researchers in strategy, economics and finance. The identified factors of performance variations have usually ranged from the industry match (complementary of assets, similarities of markets and products, synergies in production, strategic orientation, etc.), pricing policy, financing and size of the operation and type of the transaction, bidding conditions, etc.

By contrast to quantitative measurements from finance and economics, the research, which has focused on the organizational and human side of M&As, has mostly dealt with identifying factors that might have played a role in the integration process of the merging entities and led to successful outcomes. Despite the absence of a direct causal correlation, several dimensions have been identified as having an important impact on M&A performance, these include psychological, cultural and managerial factors, knowing that the human factor covers at the same time employees and managers of the companies.

Psychological Factors

A large part of the existing research has looked at the psychological effects of M&A on employees. Scholars have pointed out that strong impact that the operations could have on employees, in particular the resulting increase in stress and anxiety due to changes in work practices and tasks, managerial routines, colleagues environment, the hierarchy, etc. Further, merger and acquisitions often introduce an environment of uncertainty among employees about job losses and future career development. It has been pointed out that stress and insecurity may lead to employee resistance to change, absenteeism and lack of commitment to work and the organisation. Employee resistance prevents the building up of a well functioning organisation and constructive cooperative environment. Lack of work commitments have a negative impact on individual and organizational performance measured in terms of productivity, quality, and service. Moreover, a relationship between organizational and financial performance has also been identified which may have consequences for the market value of company.

On the other hand, it has been argued that satisfied employees are presumed to work harder, better, and longer with higher productivity records. Even though a direct relationship between job satisfaction and corporate performance remains to be established with certainty, it appears that lower job satisfaction is a cause of higher absenteeism, which, in turn is shown to have a negative influence on organizational performance.

Cultural factors
Cultural differences look like playing both ways. Although distant cultural environments make the integration process harder, the lack of culture-fit or cultural compatibility has often been used to explain M&A failure. Cultural differences have also been considered a source of lower commitment to work, making co-operation more difficult, particularly from employees of the acquired company. In this regard, scholars have largely given account of the lack of co-operation momentum stemming from a “we” versus “them” attitude, resulting in hostility among employees.

It is, therefore, no surprise that strong cultural differences are usually associated with a negative impact on M&A performance, since the integration process is less easy and deals with higher employee resistance, communication problems, and lower interest in co-operation. Noticeably, cultural clashes are likely to be more prominent in cross-national than domestic acquisitions, since such mergers bring together not only two companies that have different organizational cultures but also organizational cultures rooted in national diversity. The scholars have identified building up of a common culture as essential for the success of merger and acquisitions. Researchers have found that high levels of employees’ social identification with the organization’s identity results in increased work effort, higher performance, reduced staff turnover and more frequent involvement in positive organizational citizenship.

VI. TAKE OVER DEFENSES

Hostile takeovers directly made to the shareholders of target company has resulted in a multiple defensive strategies by corporate from being taken over by the company.

Few of the defensive strategies are as follows.

1. Packman Defense
   Under this strategy target company attempts to purchase the shares of acquirer company provided it has substantial cash flow or liquidable asset.

2. Shark Repellants
   An increasingly used defense mechanism being used is anti-takeover amendments to the company’s Articles of Association which is called shark repellants.

3. Poison pills
   Creation of securities (which is also called poison pills) which provide their holders with special rights exercisable only after a period of time following the occurrences of triggering event.

4. Refusal by the Board to register a transfer is also being adopted as a defensive strategy.

VII. PENAL PROVISIONS

Penalty for non-compliance of the provisions of SEBI (Substantial Acquisition of Shares & Takeover) Regulations, 1997, are covered under Regulation 45.

As per regulation 45, failure to carry out obligations under this regulations, may result in the following consequences:
1. The acquirer or any person acting in concert faces the consequences of the escrow amount being forfeited besides penalties.

2. The Board of Directors of Target Company shall be liable for action in terms of regulation and Act.

3. The intermediary would face suspension or cancellation of registration as member of stock exchange.

The penalties stated above may include:
(i) Criminal prosecution under section 24 of the SEBI Act.
(ii) Monetary penalties under section 15H of the SEBI Act.
(iii) Directions under section 11B of the SEBI Act.
(iv) Directions under section 11(4) of the Act;
(v) Cease and desist order in proceedings under section 11D of the Act;
(vi) Adjudication proceedings under section 15HB of the Act.

ANNEXURE A

DETAILS/DOCUMENTS/INFORMATION REQUIRED FROM TARGET COMPANY

<table>
<thead>
<tr>
<th>S. No.</th>
<th>Documents/Informations</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Certified True Copy of Memorandum &amp; Articles of Association</td>
<td></td>
</tr>
<tr>
<td>2.</td>
<td>Address of the Registered office of the Company along with Phone and Fax no.(s) (Certified Copy of Form No. 18) along with an undertaking from the Company that the registered office of the Company is situated at__________ as on date.</td>
<td></td>
</tr>
<tr>
<td>3.</td>
<td>Name of the Promoters of the Company as on date as per the definition provided in SEBI (SAST) Regulations.</td>
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<td>4.</td>
<td>The group to which it belongs.</td>
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<tr>
<td>5.</td>
<td>Details of partly Paid Up Shares of the Company, if any.</td>
<td></td>
</tr>
<tr>
<td>7.</td>
<td>Composition of Board of Directors of the company along with their designation, date of appointment, education qualification/Experience in no. of years, No. of shares held in the Company and residential address (Certified Copies of Form No. 32)</td>
<td></td>
</tr>
<tr>
<td>8.</td>
<td>Name of company Promoted by Target Company, if any.</td>
<td></td>
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<tr>
<td>10.</td>
<td>Audited Annual A/c’s of last three years and latest quarter, if applicable, of the Company.</td>
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<tr>
<td>11.</td>
<td>Status of stock exchange compliance (To be taken from all the</td>
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<tr>
<td>12.</td>
<td>Stock market data for last 6 months (To be taken from all the Stock Exchanges where the securities of the Company are Listed) and in case of infrequently traded, a certificate from the concerned Stock Exchange regarding the Last Traded Date and Price.</td>
<td></td>
</tr>
<tr>
<td>13.</td>
<td>Status of chapter II compliance (Certified Copy of letters addressed to the Company and Stock Exchanges).</td>
<td></td>
</tr>
<tr>
<td>14.</td>
<td>Latest shareholding pattern (Certified Copy of letters addressed to the Stock Exchanges).</td>
<td></td>
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<tr>
<td>15.</td>
<td>No. of shareholders in public category.</td>
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<tr>
<td>16.</td>
<td>Prospectus copy, including date of listing, date of permission for trading.</td>
<td></td>
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<tr>
<td>17.</td>
<td>Details of any other issue (bonus/right/preferential)</td>
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<tr>
<td>18.</td>
<td>Proof of payment of listing fee with all Stock Exchanges.</td>
<td></td>
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<tr>
<td>19.</td>
<td>Whether shares are in DEMAT Mode, if yes, name of the Depositories.</td>
<td></td>
</tr>
<tr>
<td>20.</td>
<td>Approvals/NOC from FIs/Banks etc.</td>
<td></td>
</tr>
<tr>
<td>21.</td>
<td>Details of litigations pending against the Company.</td>
<td></td>
</tr>
<tr>
<td>22.</td>
<td>Copy of RBI approval for allotment of Shares to NRI shareholders.</td>
<td></td>
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<tr>
<td>23.</td>
<td>Undertaking regarding non prohibition from dealing in securities by SEBI.</td>
<td></td>
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<tr>
<td>24.</td>
<td>Details of merger, De-merger, spin off etc. during last 3 years of Target Company.</td>
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<tr>
<td>25.</td>
<td>List of shareholders as on date along with their shareholding.</td>
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<tr>
<td>26.</td>
<td>Copy of Income Tax Return of all the directors &amp; Promoters for the last three years.</td>
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<tr>
<td>27.</td>
<td>Income Tax Filing of the Company.</td>
<td></td>
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<tr>
<td>28.</td>
<td>Details of Other Companies promoted by the promoters &amp; directors of the Company along with an undertaking from each director stating that no other company other than those specified have been promoted by them.</td>
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<tr>
<td>29.</td>
<td>Name of Compliance Officer of the company along with his address and contact numbers.</td>
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<tr>
<td>30.</td>
<td>Figures of the Audited Financial Results of the last 3 years and of the latest Quarter, if applicable in the prescribed Format.</td>
<td></td>
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<tr>
<td>31.</td>
<td>Complete list of investments by the Target Company.</td>
<td></td>
</tr>
<tr>
<td>32.</td>
<td>Capital Structure of the Company since inception.</td>
<td></td>
</tr>
<tr>
<td>33.</td>
<td>Copy of Disclosure under Regulation 7(1) or 7(1A) and 7(3) as the case may be filed with the Stock Exchange(s) (after entering into SPA).</td>
<td></td>
</tr>
<tr>
<td>34.</td>
<td>Copy of agreement with the Registrar/DP and his registration details (i.e. certified copy of registration certificate obtained from SEBI and a declaration that they are not prohibited by SEBI from dealing in securities).</td>
<td></td>
</tr>
<tr>
<td>35.</td>
<td>Annual Return along with all annexures (floppy, List of shareholders etc.) filed with ROC from 1997 onwards.</td>
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<tr>
<td>36.</td>
<td>Up to date ROC filing including approved DINs for all directors.</td>
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<tr>
<td>37.</td>
<td>All registrations, regulatory licenses and approvals.</td>
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<tr>
<td>39.</td>
<td>Fixed assets details.</td>
<td></td>
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<tr>
<td>40.</td>
<td>Listing Compliances and updated stock exchanges files.</td>
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</tr>
<tr>
<td>41.</td>
<td>Shareholding of the promoters along with the list of promotes, PACs and their group and any changes in shareholding and disclosures thereof. Whether the applicable provisions of the Chapter II of Takeover Code have been complied with by the <strong>Promoters, Directors, Sellers and any other major Shareholder</strong>.</td>
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<tr>
<td>42.</td>
<td>Declarations, confirmations, undertakings and other documents under SEBI.</td>
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<tr>
<td>43.</td>
<td>Listing confirmation letters from all stock exchanges.</td>
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<tr>
<td>44.</td>
<td>Details of changes in Board of Directors since inception, DOB, Qualifications, experience, date of appointment.</td>
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<tr>
<td>45.</td>
<td>Capital Structure since inception of the Company.</td>
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<tr>
<td>46.</td>
<td>SEBI file and penalties, show-cause notices, and prosecution past and pending.</td>
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<tr>
<td>47.</td>
<td>Other relevant papers, if any.</td>
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</table>

**ANNEXURE B**
CHECK LIST FOR TAKE OVER

Documents and Details to be furnished:

Acquirer/PAC:

1. Name, address and phone nos., of all Acquirers and PACs.
2. Present shareholding, if any, of the acquirer/PAC in the Target Company.
3. Brief Background of Acquirer(s) including PAC.
   The Acquire is a Company incorporate under Companies Act, 1956 to carry on the business of non banking financial activity and registered with Reserve Bank of India vide Certificate No………..
4. Copy of Agreement if any between acquirers and PACs:
5. In case acquirer(s) is a company(ies):
   (i) Name of its promoters and/or persons having control over it as the case may be, and the group to which they belong.
   (ii) Name and Residential Addresses of Board of Directors of acquirer along with their experience, qualifications, date of appointment.

<table>
<thead>
<tr>
<th>Name</th>
<th>Address</th>
<th>Qualification</th>
<th>Experience</th>
<th>DOA</th>
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</table>

(iii) Name, Address (Registered and Corporate Office) and Phone Nos.
(iv) Certificate of incorporation, Memorandum and Articles of Association of the Acquirer, in case Acquirer is a company.
(v) Brief History & Major areas of Operations: Non Banking Finance Company.
(vi) Identity of promoters and/or persons having control over such company.
(vii) Whether any Director of the Acquirer is a Director on the Board of Target Company.
(viii) Please submit the audited accounts of the last three years.
(ix) In case more than six months have elapsed since the last audited accounts then furnish the un-audited financials duly certified by the Auditor.
(x) Please give details of the major contingent liabilities and the reasons for rise/all in the total income and Profit After Tax in the relevant years.
(xi) Whether the Company had become a Sick Industrial Company anytime since its inception, if so, details thereof.

4. In case the acquirer is an individual:
   (i) Principal areas of business and relevant experience.
   (ii) Net worth duly certified by a Chartered Accountant.
(iii) Positions held on the Board of Directors of any listed company.
(iv) Name(s) of the company(ies) where the individual is a full time Director.

5. If the acquirer made any acquisitions earlier in the target company including acquisitions made through open offers, please furnish the details of changes in Shareholding pattern of the Target Company pursuant to such acquisition. What is the Status of compliance with the applicable provisions of the takeover code and any other statutory requirements?

6. If the Acquirer was required to comply with applicable provisions of Chapter II of Takeover Regulation (Disclosures), please provide details of the compliance including whether the said provisions were complied with the specified time.

7. What is the Relationship, if any, between the acquirer and Person acting in concert with it.

8. A brief write-up on Line of business and experience.

9. Whether the Acquirers intend to dispose or otherwise encumber any assets of Target Company in succeeding two years except in ordinary course of business of the target company.

10. What is the future plan about Target Company; please specify the same and how acquirer proposes to implement such future plans. Will be provided.

11. Any Statutory approvals, which are required for the purpose of acquisition of shares under the offer and also the status of the applications made in that regard.

12. Whether any approval is required from FIs/Banks for the offer.

13. Any other details pertaining to the offer or acquisition prior to offer, which is considered relevant from the shareholders' point of view.

14. Sources of Finance for the acquisition: Internal Resources.

15. Certificate from a Chartered Accountant certifying the adequacy of financial resources of the acquirer for fulfilling all the obligations under the offer.

16. Please furnish Copy of Non-Compete Agreement, if any.

17. General Risk Factors related to the open offer, and probable risks involved in associating with the Acquirer.


Documents and Details to be furnished:

Target Company:

1. Name of the Target Company:

2. Recent name changes, if any:

3. Date of incorporation:
4. Address of registered office and corporate office along with its telephone and fax numbers.

5. Brief history & Main areas of operations.
   Non Banking Financial Company


7. Please provide the locations and other details of the manufacturing facilities:

8. Please provide the Share Capital Structure of the Company in the following format:

<table>
<thead>
<tr>
<th>Paid up Equity Shares of Target Company</th>
<th>No. of Shares/voting rights</th>
<th>% of shares/voting rights</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fully paid up equity shares</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Partly paid up equity shares</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total paid up equity shares</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total voting rights in Target company</td>
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<td></td>
</tr>
</tbody>
</table>

9. Details of any partly paid shares:

10. Name of the Stock Exchange where the shares are listed, the category in which the shares are traded.

11. The annualized trading turnover in the respective SE during the preceding Six months in the following format:

<table>
<thead>
<tr>
<th>Name of stock exchange(s)</th>
<th>Total no. of shares traded during the 6 calendar months prior to the month in which PA was made</th>
<th>Total No. of listed Shares</th>
<th>Annualized Trading turnover (in terms of % to total listed shares)</th>
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</table>

12. Details of shares in Lock-in:

13. Provide details (as per the format given below) as to how the current capital structure was built since inception. Also disclose the status of compliance with the applicable provisions o Takeover Code

<table>
<thead>
<tr>
<th>Date of allotment</th>
<th>No. and % of shares issued</th>
<th>Cumulative paid up capital</th>
<th>Mode of allotment</th>
<th>Type of Issue (viz. Rights, Preferential,</th>
<th>Identity of allotees (promoters/ex-promoters/</th>
<th>Status of compliance</th>
</tr>
</thead>
<tbody>
<tr>
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</tr>
</tbody>
</table>
14. Whether the trading in the shares of the Company has been suspended in any Stock Exchange? Please specify and substantiate the steps taken to regularize the trading:

15. In case of Non-listing of some or all the shares of the Company at any Stock Exchange, please disclose the particulars thereof and the steps taken to regularize the listing. Please provide the copies of Listing Approvals.

16. Details of any outstanding convertible instruments and whether the same has been taken into account for calculating the total voting rights.

17. Shareholding of the promoters along with the list of promoters, PACs and their group and any changes in shareholding and disclosures thereof. Whether the applicable provisions of the Chapter II of Takeover Code (Disclosures) have been complied with by the Promoters, Directors, Sellers and any other major Shareholders within the specified time.

18. Whether the applicable provisions of the Chapter II of Takeover Code have been complied with by the Company within the specified time.

19. Compliance Status with Listing Agreement requirements (details to be provided year-wise since listing). Details of penal actions taken by SE, if any.

20. Give the Composition of the Board of Directors along with details of their qualification, experience, date of appointment, etc.

Composition of Board of Director

<table>
<thead>
<tr>
<th>Sl. No.</th>
<th>Name</th>
<th>DOA</th>
<th>Experience</th>
<th>Qualification</th>
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</table>

21. Was there any spin-off, merger or de-merger during the last 3 years.

22. Any change of name since its inception. Converted from Private to Public Co.

23. Dates of listing.

24. Please submit the audited accounts of the last three years.

25. In case more than six months have elapsed since the last audited accounts then furnish the un-audited financials duly certified by the Auditor for the said
26. Please give details of the major contingent liabilities and the reasons for rise/fall in the total income and Profit After Tax in the relevant years.

27. Pre and post acquisition shareholding of the target company.


29. Any pending litigations, details thereof.

30. Whether the Company had become a Sick Industrial Company anytime since its inception, if so, details thereof.


32. Name and other details of Compliance Officer of the Target Company.

33. Details of Return of Net worth, Book Value, EPS and PE Multiple, PE Multiple of Industry.

34. Market Lot of Shares in physical form.

35. Quotations from stock exchange for last 26 weeks average of weekly high and low of price of Company’s shares and last 2 weeks daily average of high and low of the shares, before the date of public announcement, at the Stock Exchanges where the shares of the Company are listed (For this purpose quotations can be directly obtained from the respective Exchanges and copies thereof may be submitted to Merchant Banker).

LESSON ROUND-UP

- A friendly takeover is with the consent of taken over company. There is an agreement between the management of two companies through negotiations and the takeover bid may be with the consent of majority or all shareholders of the target company, which is referred to as friendly takeover bid.

- When an acquirer company does not offer the target company the proposal to acquire its undertaking but silently and unilaterally pursues efforts to gain control against the wishes of existing management such acts of acquirer are known as 'takeover raids' or hostile 'takeover bids'.

- SEBI (SAST) Regulations, 1997 requires the acquirer to make a public announcement and a public offer on acquisition of a certain percentage of shares or voting rights in a company. However, certain circumstances have been provided in regulation 3, subject to which if an acquirer acquires the specified percentage of shares or voting rights, he would be exempted from the requirement of making an open offer to the existing shareholders of the company.

- Any acquirer, who acquires shares or voting rights which (taken together with shares or voting rights, if any, held by him) would entitle him to more than five per cent or ten per cent or fourteen per cent or fifty four per cent or seventy four per cent shares or voting rights in a company, in any manner whatsoever, shall disclose at every stage the aggregate of his shareholding or voting rights in that company to the company and to the stock exchanges where shares of the target company are listed.

- Any acquirer whose existing holding is between 15% to 55% of the shares or voting rights in a company (as referred in regulation (11(1)), shall disclose purchase or sale aggregating two per cent or more of the share capital of the company.
target company to the target company, and the stock exchanges where shares of
the target company are listed within two days of such purchase or sale along with
the aggregate shareholding after such acquisition or sale.

• Every person, including a person mentioned in regulation 6 (i.e., transitional
provisions relating to shares acquired before SEBI (SAST) Regulations, 1997
came into force) who holds more than fifteen per cent shares or voting rights in
any company, shall, within 21 days from the financial year ending March 31,
make yearly disclosures to the company, in respect of his holdings as on 31st
March.

• A promoter or every person having control over a company shall, within 21 days
from the financial year ending March 31, as well as the record date of the
company for the purposes of declaration of dividend, disclose the number and
percentage of shares or voting rights held by him and by persons acting in
concert with him, in that company to the company.

• Every company whose shares are listed on a stock exchange, shall within 30
days from the financial year ending March 31, as well as the record date of the
company for the purposes of declaration of dividend, make yearly disclosures to
all the stock exchanges on which the shares of the company are listed, the
changes, if any, in respect of acquirer/promoter (i.e., the holdings of the persons
referred to under sub-regulation (1) of SEBI (SAST) Regulations, 1997) and also
holdings of promoters or person(s) having control over the company, as on 31st
March.

• Trigger point is a point where provisions of SEBI (SAST) Regulations, 1997 i.e
takeover code gets triggered and the acquirer is required to follow public
announcement and other requirements as mentioned in the regulations in respect
of further acquisition.

• An acquirer who intends to acquire shares which along with his existing
shareholding would entitle him to exercise 15% or more voting rights, can acquire
such additional shares only after making a public announcement (PA) to acquire
at least additional 20% of the voting capital of Target Company from the
shareholders through an open offer.

• An acquirer who holds 15% or more but less than 55% of shares or voting rights
of a target company, can acquire such additional shares as would entitle him to
exercise more than 5% of the voting rights in any financial year ending March 31
only after making a public announcement to acquire at least additional 20% shares
of target company from the shareholders through an open offer.

• An acquirer who holds 55% or more but less than 75% shares or voting rights
of a target company, can acquire further shares or voting rights only after making a
public announcement to acquire at least additional 20% shares of target company
from the shareholders through an open offer.

• There are several obligations/compliances to be fulfilled by the acquirer, target
company and merchant banker at the time of taking over a company.

SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions are not to
be submitted for evaluation)

1. Briefly explain the takeover process.

2. When an acquirer is required to make a public announcement and what are
its contents?
3. Describe the procedure for operation of escrow account?
4. What transactions are exempted from takeover?
5. Draft a check list for the Board of Directors of Acquirer Company in respect of takeover.
6. As a Merchant Banker, describe the Plan of Action for a takeover?
STUDY V
COMPLIANCE OF LISTING AGREEMENT

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<td>• Important aspects of listing agreement such as publication requirements, compliance under clause 49, intimations to be sent to stock exchanges, minimum public holding, takeovers etc</td>
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I. INTRODUCTION

Under Section 9 of Securities Contracts (Regulation) Act, 1956, government has conferred such power to recognized stock exchanges to list the securities and to make necessary bye-laws.

The listing of securities is ensured by way of an agreement called listing agreement which is entered into between a stock exchange and the issuing company. Listing of securities at stock exchanges provides for free transferability and ready marketability securities of the Company. The listing rules and regulations have been designed to safeguard the interests of investors and to ensure transparency through disclosures, proper supervision and control over the dealings in the conduct of listed companies in India whose securities can freely be traded through SEBI.

Listing agreement is of great importance as it provides all the terms and conditions to be complied by the company whose securities are listed on the stock exchange. Listed agreement is executed under the common seal of a company.

The Listed companies are required to make continuous disclosures to stock exchanges.

II. IMPORTANT COMPLIANCES UNDER LISTING AGREEMENT

1. Board Meeting

The Company is required to intimate to the Exchange about the Board Meeting at which proposal for Buy Back of Securities, declaration/recommendation of Dividend or issue of convertible debentures or of debentures carrying a right to subscribe to equity shares or the passing over of dividend is due to be considered atleast 7 days in advance. The Company is also required to give notice simultaneously to the Stock Exchanges in case the proposal for declaration of bonus is communicated to the Board of Directors of the company as part of the agenda papers. In case of rights issue, the company is required to give prior intimation to the exchange about the board meeting at which proposal for issue of shares on rights basis to the existing shareholders is due to be considered, atleast two days in advance.
2. Annual General Meeting & Book Closure

The Company is required to close its Transfer Books for purposes of declaration of dividend or issue of right or bonus shares or issue of shares for conversion of debentures or of shares arising out of rights attached to debentures or for such other purposes as the Exchange may agree to or require. The company has to close its Transfer Books at least once a year at the time of the Annual General Meeting if they have not been otherwise closed at any time during the year and to give to the Exchange the notice in advance of at least 7 days, or of as many days as the Exchange may from time to time reasonably prescribe, stating the dates of closure of its Transfer Books (or, when the Transfer Books are not to be closed, the date fixed for taking a record of its shareholders or debenture holders) and specifying the purpose or purposes for which the Transfer Books are to be closed (or the record is to be taken) and to send copies of such notices to the other recognised stock exchanges in India. The minimum time gap between the two book closures and/or record dates has to be at least 30 days.

3. In-principle approval before further issue of shares

The company is required to obtain ‘in-principle’ approval for listing from the exchanges having nationwide trading terminals where it is listed, before issuing further shares or securities. Where the company is not listed on any exchange having nationwide trading terminals, it agrees to obtain such ‘in-principle’ approval from all the exchanges in which it is listed before issuing further shares or securities. The company agrees to make an application to the Exchange for the listing of any new issue of shares or securities and of the provisional documents relating thereto.

4. Intimation/submissions to Stock Exchange

— The Company is required to notify the Exchange of any attachment or prohibitory orders restraining the Company from transferring securities.

— The company is required to intimate to the stock exchange within 15 minutes of closure of Board meeting, by Letter/fax/telegram the following

(a) all dividends and/or cash bonuses recommended or declared or the decision to pass any dividend or interest payment;

(b) the total turnover, gross profit/loss, provision for depreciation, tax provisions and net profits for the year (with comparison with the previous year) and the amounts appropriated from reserves, capital profits, accumulated profits of past years or other special source to provide wholly or partly for the dividend, even if this calls for qualification that such information is provisional or subject to audit.

(c) the decision on Buyback of Securities.

(d) short particulars of any increase of capital whether by issue of bonus shares through capitalization, or by way of right shares to be offered to the shareholders or debenture holders, or in any other way;

(e) short particulars of the reissue of forfeited shares or securities, or the issue of shares or securities held in reserve for future issue or the creation in any form or manner of new shares or securities or any other rights, privileges or benefits to subscribe to;

(f) short particulars of any other alterations of capital, including calls;
any other information necessary to enable the holders of the listed
securities of the Company to appraise its position and to avoid the
establishment of a false market in such listed securities.

Is required to notify the exchange at least 2 days in advance of the date of
the meeting of its Board of Directors at which the the proposal for buy-back is
considered, recommendation or declaration of a dividend or convertible
debentures or of debentures carrying a right to subscribe to equity shares or
the passing over of the dividend or the issue of right is due to be considered
and will recommend or declare all dividend and/or cash bonuses at least five
days before commencement of the closure of its transfer books or the record
date fixed for the purpose.

— The Company is required to notify the Exchange at least twenty-one days in
advance of the date on and from which the dividend on shares, interest on
debentures and bonds, and redemption amount of redeemable shares or of
debentures and bonds will be payable and will issue simultaneously the
dividend warrants, interest warrants and cheques for redemption money of
redeemable shares or of debentures and bonds, which shall be payable at
par at such centres as may be agreed to between the Exchange and the
Company and which shall be collected at par, with collection charges, if any,
being borne by the Company, in any bank in the country at centres other than
the centres agreed to between the Exchange and the Company, so as to
reach the holders of shares, debentures or bonds on or before the date fixed
for payment of dividend, interest on debentures or bonds or redemption
money, as the case may be.

— The company is required to file any scheme/petition proposed to be filed
before any Court or Tribunal under sections 391,394 and 101 of the
Companies Act, 1956, with the stock exchange, for approval, at least a
month before it is presented to the Court or Tribunal.

— In the event of the Company granting any options to purchase any
shares of the Company, the Company is required to notify the
Exchange—

(a) of the number of shares covered by such options, of the terms
thereof and of the time within which they may be exercised;

(b) of any subsequent changes or cancellation or exercise of such
options.

— The Company should not make any change in the form or nature of any of its
securities that are listed on the Exchange or in the rights or privileges of the
holders thereof without giving twenty one days’ prior notice to the Exchange
of the proposed change and making an application for listing of the securities
as changed if the Exchange shall so require.

— The Company should promptly notify the Exchange of any proposed change
in the general character or nature of its business, of any change in the
Company’s directorate, of any change of Managing Director, Managing
Agents or Secretaries and Treasurers of any change of Auditors appointed to
audit the books and accounts of the Company.
— The Company is required to forward to the Exchange promptly and without application six copies of the Statutory and Directors’ Annual Reports, Balance Sheets and Profit and Loss Accounts and of all periodical and special reports as soon as they are issued and one copy each to all the recognised stock exchanges in India; six copies of all notices, resolutions and circulars relating to new issue of capital prior to their despatch to the shareholders;) three copies of all the notices, call letters or any other circulars including notices of meetings convened u/s 391 or section 394 read with section 391 of the Companies Act, 1956 together with Annexures thereto, at the same time as they are sent to the shareholders, debenture holders or creditors or any class of them or advertised in the Press;) copy of the proceedings at all Annual and Extraordinary General Meetings of the Company; three copies of all notices, circulars, etc., issued or advertised in the press either by the Company, or by any company which the Company proposes to absorb or amalgamate, or under orders of the court or any other statutory authority in connection with any merger, amalgamation, re-construction, reduction of capital, scheme or arrangement, including notices, circulars, etc. issued or advertised in the press in regard to meetings of shareholders or debenture holders or creditors or any class of them and copies of the proceedings at all such meetings.

— The Company is required to forward to the Exchange copies of all notices sent to its shareholders with respect to amendments to its Memorandum and Articles of Association and will file with the Exchange six copies (one of which will be certified) of such amendments as soon as they shall have been adopted by the Company in general meeting.

— The Company is required to intimate to the Stock Exchanges, immediately of events such as strikes, lock outs, closure on account of power cuts, etc. and all events which will have a bearing on the performance/operations of the company as well as price sensitive information both at the time of occurrence of the event and subsequently after the cessation of the event.

— The company is required to inform to stock exchange about material events such as Change in the general character or nature of business, Disruption of operations due to natural calamity, Commencement of Commercial Production/Commercial Operations, Developments with respect to pricing/realisation arising out of change in the regulatory framework, Litigation/dispute with a material impact, Revision in Ratings etc.

5. Minimum Holdings

All listed companies, other than those mentioned hereunder, is required to ensure minimum level of public shareholding at 25% of the total number of issued shares of a class or kind for the purpose of continuous listing:

(a) Companies which, at the time of initial listing, had offered less than 25% but not less than 10% of the total number of issued shares of a class or kind, in terms of Rule 19(2) (b) of Securities Contract (Regulation) Rules 1957 (SCRR) or companies desiring to list their shares by making an Initial Public Offering (IPO) of at least 10% in terms of Rule 19(2)(b) of SCRR.
(b) Companies which have, irrespective of the percentage of their shares with public at the time of initial listing, reached a size of two crore or more in terms of number of listed shares and Rs. 1000 crore or more in terms of market capitalization.

The companies at (a) and (b) above will be required to maintain the minimum level of public shareholding at 10% of the total number of issued shares of a class or kind for the purpose of continuous listing.

6. Company Secretary as Compliance Officer

The Company is required to appoint the Company Secretary to act as Compliance Officer who will be responsible for monitoring the share transfer process and report to the Company’s Board in each meeting. The compliance officer will directly liaise with the authorities such as SEBI, Stock Exchanges, Registrar of Companies, etc., and investors with respect to implementation of various clauses, rules, regulations and other directives of such authorities and investor service and complaints of related matter. He is also responsible for ensuring the correctness, authenticity and comprehensiveness of the information, statements and reports filed under clause 52 pertaining to Corporate Filing and Dissemination System (CFDS), and also for ensuring that such information is in conformity with the applicable laws and the listing agreement.

7. Financial results/Publications

1. Preparation and Submission of Financial Results

— Financial Results filed/published shall be prepared on the basis of accrual policy and in accordance with uniform accounting practices adopted for all the periods.

— Company has the option to submit audited/unaudited quarterly financial results within one month from the end of quarter, except for the last quarter.

(a) Companies are required submit a copy of the limited review report to the stock exchange within two months from end of the quarter, in case the company opts to submit unaudited financial results.

(b) Financial results are to be accompanied by auditors report in case the company opts to submit audited financial results

— In case of last quarter, the company has the following options.

i.e. the company is required to submit either unaudited financial results for the quarter within one month of end of the financial year or to submit audited financial results for the entire financial year within three months of end of the financial year, subject to the following:

(a) In case the company opts to submit un-audited financial results for the last quarter, it shall also submit audited financial results for the entire financial year, as soon as they are approved by the Board. Such un-audited financial results for the last quarter shall also be subjected to limited review by the statutory auditors of the company (or in case of public sector undertakings, by any practicing Chartered Accountant) and a copy of the limited review report shall be furnished to the stock
exchange within two months from end of the quarter.

(b) The company is required to intimate the option to the stock exchange in writing within one month of end of the financial year, in case the company opts to submit audited financial results for the entire financial year.

— Companies having subsidiaries may, in addition to submitting quarterly and year to date stand alone financial results to the stock exchange also submit quarterly and year to date consolidated financial results within two months from end of the quarter; and while submitting annual audited financial results prepared on stand-alone basis, it shall also submit annual audited consolidated financial results to the stock exchange.

— The company is required to submit financial results to the stock exchange within fifteen minutes of conclusion of the meeting of the Board or Committee in which they were approved.

2. Manner of approval and authentication of the financial results

— The quarterly financial results submitted shall be approved by the Board of Directors of the company or by a committee thereof, other than the audit committee. When the quarterly financial results are approved by the Committee they shall be placed before the Board at its next meeting:

— While placing the financial results before the Board, the Chief Executive Officer and Chief Financial Officer of the company, by whatever name called, shall certify that the financial results do not contain any false or misleading statement or figures and do not omit any material fact which may make the statements or figures contained therein misleading.

— The financial results submitted to the stock exchange shall be signed by the Chairman or managing director, or a whole time director. In the absence of all of them, it shall be signed by any other director of the company who is duly authorized by the Board to sign the financial results.

— The limited review report to be placed before the Board of directors or the Committee before being submitted to the stock exchange where the variation between unaudited financials and financial amended pursuant to limited review exceeds 10%. When the limited review report is placed before the Committee they shall also be placed before the Board at its next meeting.

— The annual audited financial results shall be approved by the Board of Directors of the company and shall be signed.

3. Intimation of Board Meeting relating to financial results

— The company is required to give prior intimation of the date and purpose of meetings of the Board or Committee in which the financial results will be considered at least seven clear calendar days prior to the meeting (excluding the date of the intimation and date of the meeting).

— The Company is also required to issue a public notice in at least in one English daily newspaper circulating in the whole or substantially the whole of India and in one daily newspaper published in the language of the region, where the registered office of the company is situated.
4. **Publication of financial results in newspapers**

The company shall, within 48 hours of conclusion of the Board or Committee meeting at which the financial results were approved, publish a copy of the financial results which were submitted to the stock exchange in at least one English daily newspaper circulating in the whole or substantially the whole of India and in one daily newspaper published in the language of the region, where the registered office of the company is situated:

— Where the company has opted to submit audited financial results, it shall also publish the qualifications or reservations, if any, expressed by the auditor together with the audited results

— Where the company has submitted consolidated financial results in addition to stand-alone financial results, it shall have an option to publish either stand-alone financial results or consolidated financial results in the newspapers, subject to the following:

(i) It shall intimate the stock exchange in the first quarter of the financial year or within such extended period as may be specified by SEBI in this regard and shall not change the same during the financial year;

(ii) In case the company changes its option in any subsequent year, it shall furnish comparable figures for the previous year in accordance with the option exercised for the current year;

(iii) It shall give a reference in the newspaper publication, to the places, such as the company’s website and stock exchanges’ websites, where the standalone results of the company are available.

5. **Other issue requirements relating to financial results**

— Where there is a variation between the unaudited quarterly or year to date financial results and the results amended pursuant to limited review for the same period, and –

(a) the variation in net profit or net loss after tax is in excess of 10% or Rs.10 lakhs, whichever is higher; or

(b) the variation in exceptional or extraordinary items is in excess of 10% or Rs.10 lakhs, whichever is higher

— The company shall submit to the stock exchange an explanation of the reasons for variations, while submitting the limited review report. The explanation of variations so submitted shall be approved by the Board of Directors:

— If the auditor has expressed any qualification or other reservation in respect of audited financial results submitted or published under this clause, the company shall disclose such qualification or other reservation and impact of the same on the profit or loss, while publishing or submitting such results.

— If the auditor has expressed any qualification or other reservation in his audit report or limited review report in respect of the financial results of
any previous financial year or quarter which has an impact on the profit or loss of the reportable period, the company shall include as a note to the financial results –

(i) how the qualification or other reservation has been resolved; or

(ii) if it has not been resolved, the reason therefor and the steps which the company intends to take in the matter.

— If the company has changed its name suggesting any new line of business, it shall disclose the net sales or income, expenditure and net profit or loss after tax figures pertaining to the said new line of business separately in the financial results and shall continue to make such disclosures for the three years succeeding the date of change in name.

— If the company had not commenced commercial production or commercial operations during the reportable period, the company shall, instead of submitting financial results, disclose the details of amount raised, the portions thereof which is utilized and that remaining unutilized, the details of investment made pending utilisation, brief description of the project which is pending completion, status of the project and expected date of commencement of commercial production or commercial operations.

8. Statement of deviations and appointment of monitoring agency.

The company has to appoint a monitoring agency to monitor utilisation of proceeds of public/rights issue and deviations if any in the usage of funds has to be intimated to the stock exchange on quarterly basis, and such statement of deviation has to be filed with quarterly/annual financial results filed under clause 41. It should also be published in newspapers simultaneously with financial results after placing the same before audit committee.

9. Shareholding Pattern

The company is required to file shareholding pattern with the Exchange on a quarterly basis, within 21 days from the end of each quarter, in the format specified.

10. Uniform procedure for dealing with unclaimed shares

As there is a large quantum of shares issued pursuant to the public issues, which remain unclaimed despite the best efforts of the Registrar to Issue or Issuers Clause 5A has been inserted to listing agreement for providing a uniform procedure for dealing with unclaimed shares i.e., shares which could not be allotted to the rightful shareholder due to insufficient/incorrect information or any other reason.

Accordingly, the new Clause 5A is, which, inter alia, provides the following:

(a) The unclaimed shares shall be credited to a demat suspense account opened by the issuer with one of the depository participants.

(b) Any corporate benefit in terms of securities, accruing on unclaimed shares such as bonus shares, split etc., shall also be credited to such account.

(c) Details of shareholding of each individual allottee whose shares have been credited to such suspense account shall be properly maintained by the issuer.

(d) The allottee’s account shall be credited as and when he/she approaches the
issuer, after undertaking the proper verification of identity of the allottee.

(e) The voting rights of these shares will remain frozen till the rightful owner claims the shares.

(f) Details of shares in aggregate in the suspense account including freeze on their voting rights, shall be disclosed in the Annual Report as long as there are shares in the suspense account

11. Corporate Governance

Clause 49 of the Listing Agreement contains provisions relating to Good Corporate Governance practices. The salient features of clause 49 are given below.

1. Independent Director

The Board of directors of the company shall have an optimum combination of executive and non-executive directors with not less than fifty percent of the board of directors comprising of non-executive directors.

Where the Chairman of the Board is a non-executive director, at least one-third of the Board should comprise of independent directors and in case he is an executive Director, at least half of the Board should comprise of independent directors.

If the non-executive Chairman is a promoter or is related to promoters or persons occupying management positions at the board level or at one level below the board, at least one-half of the board of the company should consist of independent directors.

‘Independent director’ means a non-executive director of the company who:

(a) apart from receiving director’s remuneration, does not have any material pecuniary relationships or transactions with the company, its promoters, its directors, its senior management or its holding company, its subsidiaries and associates which may affect independence of the director;

(b) is not related to promoters or persons occupying management positions at the board level or at one level below the board;

(c) has not been an executive of the company in the immediately preceding three financial years;

(d) is not a partner or an executive or was not partner or an executive during the preceding three years, of any of the following:

(i) the statutory audit firm or the internal audit firm that is associated with the company, and

(ii) the legal firm(s) and consulting firm(s) that have a material association with the company.

(e) is not a material supplier, service provider or customer or a lessor or lessee of the company, which may affect independence of the director;

(f) is not a substantial shareholder of the company i.e. owning two percent or more of the block of voting shares.

(g) is not less than twenty one years of age.

An independent director who resigns or is removed from the Board of the Company shall be replaced by a new independent director within a period of not more than 180 days from the day of such resignation or removal, as the case may be. However, if the company fulfils the requirement of independent directors in its Board
even without filling the vacancy created by such resignation or removal, as the case may be, the requirement of replacement by a new independent director within the period of 180 days shall not apply.

2. Nominee Directors

Nominee directors appointed by an institution which has invested in or lent to the company shall be deemed to be independent directors.

3. Non executive directors’ compensation and disclosures

All fees/compensation, if any paid to non-executive directors, including independent directors, shall be fixed by the Board of Directors and require previous approval of shareholders in general meeting. However, prior approval of shareholders in general meeting shall not apply to payment of sitting fees to non-executive directors, if made within the limits prescribed under the Companies Act, 1956 for payment of sitting fees without approval of the Central Government.

4. Board Meetings

The Board shall meet at least four times a year with a maximum time gap of four months between any two meetings. The Clause prescribes a list comprising minimum information to be placed before Board of Directors.

5. No of Directorships

A director shall not be a member in more than 10 committees or act as Chairman of more than five committees across all companies in which he is a director. Furthermore it should be a mandatory annual requirement for every director to inform the company about the committee positions he occupies in other companies and notify changes as and when they take place.

6. Code of conduct

The Board shall lay down a code of conduct for all Board Members and senior management of the Company and the same to be posted on the website of the company. All Board members and senior management personnel shall affirm compliance with the code on an annual basis. The Annual Report of the company shall contain a declaration to this effect signed by the CEO.

7. Subsidiary Companies

(i) At least one independent director on the Board of Directors of the holding company shall be a director on the Board of Directors of a material non-listed Indian subsidiary company.

(ii) The Audit Committee of the listed holding company shall also review the financial statements, in particular, the investments made by the unlisted subsidiary company.

(iii) The minutes of the Board meetings of the unlisted subsidiary company shall be placed at the Board meeting of the listed holding company. The management should periodically bring to the attention of the Board of Directors of the listed holding company, a statement of all significant transactions and arrangements entered into by the unlisted subsidiary company.

The term “material non-listed Indian subsidiary” means an unlisted subsidiary,
incorporated in India, whose turnover or net worth (i.e. paid up capital and free reserves) exceeds 20% of the consolidated turnover or net worth respectively, of the listed holding company and its subsidiaries in the immediately preceding accounting year.

The term “significant transaction or arrangement” means any individual transaction or arrangement that exceeds or is likely to exceed 10% of the total revenues or total expenses or total assets or total liabilities, as the case may be, of the material unlisted subsidiary for the immediately preceding accounting year.

Where a listed holding company has a listed subsidiary which is itself a holding company, the above provisions shall apply to the listed subsidiary insofar as its subsidiaries are concerned.

8. Certificate from a Company Secretary in Practice / Auditors

The company shall obtain a certificate from either the auditors or practicing company secretaries regarding compliance of conditions of corporate governance as stipulated in this clause and annex the certificate with the directors’ report, which is sent annually to all the shareholders of the company. The same certificate shall also be sent to the Stock Exchanges along with the annual report filed by the company.

9. Report on Corporate Governance

There shall be a separate section on Corporate Governance in the Annual Reports of company, with a detailed compliance report on Corporate Governance. Non-compliance of any mandatory requirement of this clause with reasons thereof and the extent to which the non-mandatory requirements have been adopted should be specifically highlighted. The clause also prescribes suggested list of items to be included in this report.

10. CEO/CFO certification

The CEO, i.e. the Managing Director or Manager appointed in terms of the Companies Act, 1956 and the CFO i.e. the whole-time Finance Director or any other person heading the finance function discharging that function shall certify to the Board that:

(a) They have reviewed financial statements and the cash flow statement for the year and that to the best of their knowledge and belief:
   (i) these statements do not contain any materially untrue statement or omit any material fact or contain statements that might be misleading;
   (ii) these statements together present a true and fair view of the company’s affairs and are in compliance with existing accounting standards, applicable laws and regulations.

(b) There are, to the best of their knowledge and belief, no transactions entered into by the company during the year which are fraudulent, illegal or violative of the company’s code of conduct.

(c) They accept responsibility for establishing and maintaining internal controls for financial reporting and that they have evaluated the effectiveness of internal control systems of the company pertaining to financial reporting and they have disclosed to the auditors and the Audit Committee, deficiencies in the design or operation of such internal controls, if any, of which they are
aware and the steps they have taken or propose to take to rectify these deficiencies.

(d) They have indicated to the auditors and the Audit committee

(i) significant changes in internal control over financial reporting during the year;

(ii) significant changes in accounting policies during the year and that the same have been disclosed in the notes to the financial statements; and

(iii) instances of significant fraud of which they have become aware and the involvement therein, if any, of the management or an employee having a significant role in the company's internal control system over financial reporting.

11. Audit Committee

(a) Requirement of Constitution of Audit Committee

All listed companies shall have a qualified and independent Audit Committee. The Audit Committee shall meet at least four times in a year and not more than four months shall elapse between two meetings.

(b) No of Directors

The audit committee shall have minimum three directors as members. Two-thirds of the members of audit committee shall be independent directors. All members of audit committee shall be financially literate and at least one member shall have accounting or related financial management expertise.

(c) Chairman of audit Committee

The Chairman of the Audit Committee shall be an independent director and shall be present at Annual General Meeting to answer shareholder queries;

(d) Special invitees

The audit committee may invite such of the executives, as it considers appropriate (and particularly the head of the finance function) to be present at the meetings of the committee, but on occasions it may also meet without the presence of any executives of the company. The finance director, head of internal audit and a representative of the statutory auditor may be present as invitees for the meetings of the audit committee.

(e) Company Secretary

The Company Secretary shall act as the secretary to the audit committee.

(f) Quorum of Audit Committee

The quorum shall be either two members or one third of the members of the audit committee whichever is greater, but there should be a minimum of two independent members present.

(g) Powers of Audit Committee

The audit committee shall have powers, which should include the following:

1. To investigate any activity within its terms of reference.

2. To seek information from any employee.
3. To obtain outside legal or other professional advice.
4. To secure attendance of outsiders with relevant expertise, if it considers necessary.

(h) Role of Audit Committee

The role of the audit committee shall include the following:

(a) Oversight of the company’s financial reporting process and the disclosure of its financial information to ensure that the financial statement is correct, sufficient and credible.

(b) Recommending to the Board, the appointment, re-appointment and, if required, the replacement or removal of the statutory auditor and the fixation of audit fees.

(c) Approval of payment to statutory auditors for any other services rendered by the statutory auditors.

(d) Reviewing, with the management, the annual financial statements before submission to the board for approval, with particular reference to:

1. Matters required to be included in the Director’s Responsibility Statement to be included in the Board’s report in terms of clause (2AA) of section 217 of the Companies Act, 1956
2. Changes, if any, in accounting policies and practices and reasons for the same
3. Major accounting entries involving estimates based on the exercise of judgment by management
4. Significant adjustments made in the financial statements arising out of audit findings
5. Compliance with listing and other legal requirements relating to financial statements
6. Disclosure of any related party transactions
7. Qualifications in the draft audit report.

(e) Reviewing, with the management, the quarterly financial statements before submission to the board for approval

(f) Reviewing, with the management, the statement of uses / application of funds raised through an issue (public issue, rights issue, preferential issue, etc.), the statement of funds utilized for purposes other than those stated in the offer document/prospectus/notice and the report submitted by the monitoring agency monitoring the utilisation of proceeds of a public or rights issue, and making appropriate recommendations to the Board to take up steps in this matter.

(g) Reviewing, with the management, performance of statutory and internal auditors, adequacy of the internal control systems.

(h) Reviewing the adequacy of internal audit function, if any, including the structure of the internal audit department, staffing and seniority of the official heading the department, reporting structure, coverage and frequency of internal audit.

(i) Discussion with internal auditors any significant findings and follow up there on.
(j) Reviewing the findings of any internal investigations by the internal auditors into matters where there is suspected fraud or irregularity or a failure of internal control systems of a material nature and reporting the matter to the board.

(k) Discussion with statutory auditors before the audit commences, about the nature and scope of audit as well as post-audit discussion to ascertain any area of concern.

(l) To look into the reasons for substantial defaults in the payment to the depositors, debenture holders, shareholders (in case of non payment of declared dividends) and creditors.

(m) To review the functioning of the Whistle Blower mechanism, in case the same is existing.

(n) Carrying out any other function as is mentioned in the terms of reference of the Audit Committee.

(i) Review of information

The Audit Committee shall mandatorily review the following information:

- Management discussion and analysis of financial condition and results of operations;
- Statement of significant related party transactions submitted by the management;
- Management letters/letters of internal control weaknesses issued by the statutory auditors;
- Internal audit reports relating to internal control weaknesses; and
- The appointment, removal and terms of remuneration of the Chief Internal Auditor shall be subject to review by the Audit Committee.

12. Disclosures

The clause requires the company to make disclosures on the following aspects.

1. Basis of related party transactions
2. Disclosure of Accounting Treatment
3. Board Disclosures on Risk management
4. Proceeds from public issues, rights issues, preferential issues etc.
5. Remuneration of Directors
6. Management
7. Disclosures to Shareholders

13. Non-Mandatory Requirements

1. The Board

A non-executive Chairman may be entitled to maintain a Chairman’s office at the company’s expense and also allowed reimbursement of expenses incurred in performance of his duties.

Independent Directors may have a tenure not exceeding, in the aggregate, a period of nine years, on the Board of a company.
2. Remuneration Committee
   (i) The board may set up a remuneration committee to determine on their behalf and on behalf of the shareholders with agreed terms of reference, the company's policy on specific remuneration packages for executive directors including pension rights and any compensation payment.
   (ii) To avoid conflicts of interest, the remuneration committee, which would determine the remuneration packages of the executive directors may comprise of at least three directors, all of whom should be non-executive directors, the Chairman of committee being an independent director.
   (iii) All the members of the remuneration committee could be present at the meeting.
   (iv) The Chairman of the remuneration committee could be present at the Annual General Meeting, to answer the shareholder queries. However, it would be up to the Chairman to decide who should answer the queries.

3. Shareholder Rights
   A half-yearly declaration of financial performance including summary of the significant events in last six-months, may be sent to each household of shareholders.

4. Audit qualifications
   Company may move towards a regime of unqualified financial statements.

5. Training of Board Members
   A company may train its Board members in the business model of the company as well as the risk profile of the business parameters of the company, their responsibilities as directors, and the best ways to discharge them.

6. Mechanism for evaluating non-executive Board Members
   The performance evaluation of non-executive directors could be done by a peer group comprising the entire Board of Directors, excluding the director being evaluated; and Peer Group evaluation could be the mechanism to determine whether to extend / continue the terms of appointment of non-executive directors.

7. Whistle Blower Policy
   The company may establish a mechanism for employees to report to the management concerns about unethical behaviour, actual or suspected fraud or violation of the company’s code of conduct or ethics policy. This mechanism could also provide for adequate safeguards against victimization of employees who avail of the mechanism and also provide for direct access to the Chairman of the Audit committee in exceptional cases. Once established, the existence of the mechanism may be appropriately communicated within the organization.

The time based, event based compliance check list under listing agreement and month wise compliance checklist for a listed company is given as
Annexure A, B and C respectively.

III. PENALTY FOR NON-COMPLIANCE OF LISTING AGREEMENT

The penal provisions for non-compliance of the conditions of the Listing Agreement are governed by Clause 23(2) and Clause 23E of the Securities Contract (Regulation) Act, (SCRA) 1956.

Clause 23(2) states that any person who fails to comply with the provisions of section 21 (conditions for listing) shall without prejudice to any award of penalty by Adjudicating Officer on conviction be punishable with imprisonment for a term which may extend to ten years or with fine which may extend to twenty five crore rupees or with both.

Clause 23E of SCRA states that if any company fails to comply with the listing conditions or delisting conditions or grounds or commits a breach thereof, it shall be liable to a penalty not exceeding twenty five crore rupees.

Apart from the above, a recognized stock exchange may suspend or withdraw admission to dealings in the securities of a company or body corporate either for a breach of or non-compliance with, any of the conditions of admission to dealings or for any other reason, to be recorded in writing, which in the opinion of the stock exchange justifies such action.

The Stock Exchanges may delist companies with have been suspended for a minimum period of six months for non-compliance with the Listing Agreement. The Stock Exchange may also delist companies as per the norms provided in Schedule III of the Securities and Exchange Board of India (Delisting of Securities) Guidelines, 2003.

IV. CERTIFICATION BY PRACTISING COMPANY SECRETARY – LISTING AGREEMENT

1. Certificate under clause 47(c)
   a certificate from a practicing company secretary that all transfers has been completed within the stipulated time.

2. Certification under clause 49
   a certificate from the auditor of the company or from a practicing company secretary regarding compliance of conditions of corporate governance as stipulated in this clause.
## ANNEXURE A

### TIME BASED COMPLIANCE

<table>
<thead>
<tr>
<th>Month of Compliance/ due dates</th>
<th>Provisions of the Listing Agreement (Clause No. of the Listing Agreement)</th>
<th>Compliance requirements</th>
</tr>
</thead>
<tbody>
<tr>
<td>January</td>
<td>Shareholders’/Investors’ Transfer/ Grievance Committee Meeting to be held by the Company (8, 41 &amp; 49)</td>
<td>Approval and processing of Transfer, Transmission, Demat and issue of Duplicate Share Certificates etc. to be placed before the Committee</td>
</tr>
<tr>
<td>January</td>
<td>Audit Committee Meeting for approving the Results of the Company to be held by the company (41 &amp; 49)</td>
<td>Approval of results is required for submission of the Results to the Board</td>
</tr>
<tr>
<td>January</td>
<td>A statement is required to be prepared by the company indicating the variations between projected utilisation of funds and/or projected profitability statement made by the Company in its prospectus or letter of offer or object/s stated in the explanatory statement to the notice for the general meeting for consideration preferential issue of securities, and the actual utilisation of funds and/ or actual profitability.(43)</td>
<td>Furnish on a quarterly basis to the Exchange for each of the years for which projects are provided in the prospectus/letter of offer/ object/s stated in the explanatory statement to the notice for consideration preferential issue of securities</td>
</tr>
<tr>
<td>15th January</td>
<td>Quarterly Compliance Report on Corporate Governance to be prepared by the company and signed by the Compliance Officer or Chief Executive Officer of the Company (49(VI)(ii))</td>
<td>To be submitted to the Stock Exchange within 15 days from the end of each quarter</td>
</tr>
<tr>
<td>21st January</td>
<td>The Company is required to file the quarterly shareholding pattern in the revised format indicating the shares pledged or otherwise encumbered (35)</td>
<td>With the Stock Exchange within 21 days from the end of the quarter</td>
</tr>
<tr>
<td>23rd January</td>
<td>Notice of Board Meeting for unaudited quarterly results to be sent by the Company (41)</td>
<td>To the Stock Exchange at least 7 days prior to the Board Meeting</td>
</tr>
<tr>
<td>Date</td>
<td>Event Description</td>
<td>Deadline</td>
</tr>
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</tr>
<tr>
<td>23rd January</td>
<td>The Company is required to issue press release in at least one national newspaper and one regional language newspaper about the date of the Board or its Sub Committee Meeting for un-audited quarterly results. (41)</td>
<td>At least 7 days prior to the Board Meeting</td>
</tr>
<tr>
<td>23rd January</td>
<td>Notice of Board Meeting to make additional quarterly disclosures as prescribed under Schedule VI of the Companies Act, 1956, is required to be sent where the company has not yet commenced its commercial production. (41)</td>
<td>To the Stock Exchange at least 7 days prior to the Board Meeting</td>
</tr>
<tr>
<td>23rd January</td>
<td>The Company is required to issue press release in at least one national newspaper and one regional language newspaper about the date of the Board or its Sub Committee Meeting to make additional quarterly disclosures as prescribed under Schedule VI of the Companies Act, 1956. (41)</td>
<td>At least 7 days prior to the Board Meeting</td>
</tr>
<tr>
<td>30th January</td>
<td>Board Meeting to be held by the Company where the company has not yet commenced its commercial production, it will make additional quarterly disclosures as prescribed under Schedule VI of the Companies Act, 1956, for the balance of utilization of monies raised by issue and the form in which such utilization funds have been invested by the issuer. (41)</td>
<td>Board Meeting to be held within 1 month. Disclosures to be sent to the Stock Exchange</td>
</tr>
<tr>
<td>30th January</td>
<td>Board Meeting for the quarterly Results and segment wise revenue, results and capital employed report to be held by the Company. (41)</td>
<td>Within 1 month from the end of the quarter</td>
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</tr>
<tr>
<td>30th January</td>
<td>Intimation of quarterly results by the Company in the revised format along with segment-wise revenue, results and capital employed (41)</td>
<td>To Stock Exchanges within 15 minutes from the closure of the Board Meeting</td>
</tr>
<tr>
<td>1st February</td>
<td>Publication of quarterly results by the Company and statement of deviations in use of issue proceeds in at least one English daily newspaper circulating in the whole or substantially the whole of India and in one newspaper published in the language of the region, where the registered office of the company is situated. The Company is required to publish the number of investor complaints pending at the beginning of the quarter, received and disposed off during the quarter and lying unresolved at the end of the quarter (41 &amp; 43A)</td>
<td>Within 48 hours of the conclusion of the Board Meeting. Apart from the quarterly results, the statement of investor complaints and the statement of variation of utilization of funds are required to be published by the Company along with the quarterly results. For each of the years for which projects are provided in the prospectus/letter of offer/object/s stated in the explanatory statement to the notice for considering preferential issue of securities, and the actual utilization of funds and/or actual profitability. (43) Where there is a material variation, the company is required to furnish an explanation in the advertisement.</td>
</tr>
<tr>
<td>February</td>
<td>Shareholders’/Investors’ Transfer/Grievance Committee Meeting to be held by the Company (8, 41 &amp; 49)</td>
<td>Approval and processing of Transfer, Transmission, Demat and issue of Duplicate Share Certificate etc. to be placed before the Committee</td>
</tr>
<tr>
<td>Date</td>
<td>Event Description</td>
<td>Action Required</td>
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<tr>
<td>28th/29th February</td>
<td>Limited Review accompanied by a statement (approved by the Board of Directors) explaining the reasons to the Stock Exchanges, if in respect of any item given in the same proforma format varies by 10% or 10 lakhs is higher from the respective unaudited quarterly results as determined after the “Limited Review” by the Auditors (41)</td>
<td>To be submitted by the Company to the Stock Exchanges. This is not required if audited quarterly results are submitted within 1 month from the end of the third quarter</td>
</tr>
<tr>
<td>March</td>
<td>Shareholders’/Investors’ Transfer/Grievance Committee Meeting to be held by the Company (8, 41 &amp; 49)</td>
<td>Approval and processing of Transfer, Transmission, Demat and issue of Duplicate Share Certificate etc. to be placed before the Committee</td>
</tr>
<tr>
<td>April</td>
<td>A statement is required to be prepared by the company indicating the variations between projected utilization of funds and/or projected profitability statement made by the Company in its prospectus or letter of offer or object/s stated in the explanatory statement to the notice for the general meeting for considering preferential issue of securities, and the actual utilization of funds and/or actual profitability (43)</td>
<td>Furnish on a quarterly basis to the Exchange for each of the years for which projections are provided in the prospectus/letter of offer/object/s stated in the explanatory statement to the notice for considering preferential issue of securities</td>
</tr>
<tr>
<td>15th April</td>
<td>Quarterly Compliance Report on Corporate Governance to be prepared by the company and signed by the Compliance Officer or Chief Executive Officer of the Company (49 VI(ii))</td>
<td>To be submitted to the Stock Exchange within 15 days from the end of each quarter</td>
</tr>
<tr>
<td>21st April</td>
<td>Declaration from the Promoters in respect of their holding as on 31st March under SEBI (SAST) Regulations (40B)</td>
<td>To be given to the Company within 21 days from the end of financial year</td>
</tr>
<tr>
<td>21st April</td>
<td>The Company is required to file the quarterly share-holding pattern in the revised format indicating therein, the details of</td>
<td>With the Stock Exchange within 21 days from the end of the quarter</td>
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<tr>
<td></td>
<td>the shares pledged or otherwise encumbered (35)</td>
<td></td>
</tr>
<tr>
<td>23rd April</td>
<td>Notice of Board Meeting for unaudited quarterly results to be sent by the Company (41)</td>
<td>To the Stock Exchange at least 7 days prior to the Board Meeting</td>
</tr>
<tr>
<td>23rd April</td>
<td>The Company is required to issue press release in at least one national newspaper and one regional language newspaper about the date of the Board or its Sub Committee Meeting for un-audited quarterly results (41)</td>
<td>At least 7 days prior to the Board Meeting</td>
</tr>
<tr>
<td>23rd April</td>
<td>Notice of Board Meeting to make additional quarterly disclosures as prescribed under Schedule VI of the Companies Act 1956, is required to be sent where the company has not yet commenced its commercial production (41)</td>
<td>To the Stock Exchange at least 7 days prior to the Board Meeting</td>
</tr>
<tr>
<td>23rd April</td>
<td>The Company is required to issue press release in at least one national newspaper and one regional language newspaper about the date of the Board or its Sub Committee Meeting to make additional quarterly disclosures as prescribed under Schedule VI of the Companies Act, 1956. (41)</td>
<td>At least 7 days prior to the Board Meeting</td>
</tr>
<tr>
<td>30th April</td>
<td>Board Meeting to be held by the Company where the company has not yet commenced its commercial production, it will make additional quarterly disclosures as prescribed under Schedule VI of the Companies Act 1956, for the balance of utilization of monies raised by issue and the form in which such utilization funds have been invested by the issuer. (41)</td>
<td>Board Meeting to be held within 1 month. Disclosures to be sent to the Stock Exchange</td>
</tr>
<tr>
<td>Date</td>
<td>Event Description</td>
<td>Date/Time Requirement</td>
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</tr>
<tr>
<td>30th April</td>
<td>Listing Fees to be paid by the Company [38(a)]</td>
<td>Annual Listing fees to be paid to the Stock Exchange computed on the basis of the capital of the Issuer as on March 31 and worked out as provided in the Listing Agreement</td>
</tr>
<tr>
<td>30th April</td>
<td>Board Meeting for the quarterly Results and segment wise revenue, results and capital employed report to be held by the Company (41)</td>
<td>Within 1 month from the end of the quarter</td>
</tr>
<tr>
<td>30th April</td>
<td>Intimation of quarterly results by the Company in the revised format alongwith segment wise revenue, results and capital employed (41)</td>
<td>To Stock Exchanges within 15 minutes from the closure of the Board Meeting</td>
</tr>
<tr>
<td>30th April</td>
<td>Submission of Half yearly Audit from a Practising Company Secretary. This is required to be submitted to the Company by the Registrar &amp; Transfer Agent (RTA) (47(c))</td>
<td>Within 1 month from the end of half year, to be submitted to the Exchange 24 hours of the receipt of the certificate by the Company</td>
</tr>
<tr>
<td>30th April</td>
<td>Intimation by the Company that it will publish audited yearly results within 3 months from the end of the last quarter of the financial year (41)</td>
<td>In advance to the Stock Exchange</td>
</tr>
<tr>
<td>May</td>
<td>Shareholders’/Investors’ Transfer/ Grievance Committee Meeting to be held by the Company (8, 41 &amp; 49)</td>
<td>Approval and processing of Transfer, Transmission, Demat and issue of Duplicate Share Certificate etc. to be placed before the Committee</td>
</tr>
<tr>
<td>May</td>
<td>Audit Committee Meeting for approving the Results of the Company to be held by the Company (41 &amp; 49)</td>
<td>Approval of results is required for submission of the Results to the Board</td>
</tr>
<tr>
<td>2nd May</td>
<td>Publication of quarterly results by the Company and Statement of deviations of issue proceeds in at least one English daily news paper circulating in the whole or substantially the whole</td>
<td>Within 48 hours of the conclusion of the Board Meeting. Apart from the quarterly results the statement of investor complaints and the statement of</td>
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<td>of India and in one newspaper published in the language of the region, where the registered office of the company is situated. The Company is required to publish the number of investor complaints pending at the beginning of the quarter, received and disposed off during the quarter and lying unresolved at the end of the quarter (41)</td>
<td>variation of utilization of funds are required to be published by the Company alongwith the quarterly results</td>
<td></td>
</tr>
<tr>
<td>The Company is required to publish the statement of variation between projected utilization of funds and/or projected profitability statement made by it in its prospectus or letter of offer or object/s stated in the explanatory statement to the notice for the general meeting for considering preferential issue of securities, and the actual utilization of funds and/or actual profitability. (43)</td>
<td>For each of the years for which projections are provided in the prospectus/letter of offer/object/s stated in the explanatory statement to the notice for considering preferential issue of securities Where there is a material variation, the company is required to furnish an explanation in the advertisement.</td>
<td></td>
</tr>
<tr>
<td>3rd or 4th week of May Board Meeting for approving the Audited Results, Declaration of Dividend, Appointment of Auditors to be held by the Company (41)</td>
<td>— At least 7 days prior intimation to the Stock Exchanges. — Publication of Audited Results for year within 3 months from the end of the year.</td>
<td></td>
</tr>
<tr>
<td>30th May Limited Review accompanied by a statement (approved by the Board of Directors) explaining the reasons to the Stock Exchanges, if in respect of any item given in the same proforma format varied by 10% or 10 lakh whichever is higher from the respective unaudited quarterly results as determined after the “Limited Review” by the Auditors (41)</td>
<td>To be submitted by the Company to the Stock Exchanges. This is not required if audited quarterly results are submitted within 1 month from the end of the third quarter</td>
<td></td>
</tr>
<tr>
<td>June Shareholders'/Investors' Transfer/ Grievance Committee Meeting to be held by the Company (8, 41 &amp; 49)</td>
<td>Approval and processing of Transfer, Transmission, Demat and issue of Duplicate Share Certificate etc. to be placed</td>
<td></td>
</tr>
<tr>
<td>Date</td>
<td>Event Description</td>
<td>Reference</td>
</tr>
<tr>
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</tr>
<tr>
<td>23rd June</td>
<td>Notice of Board Meeting for audited yearly results to be sent by the Company (41)</td>
<td>(41)</td>
</tr>
<tr>
<td>23rd June</td>
<td>The Company is required to issue press release in at least one national news paper and one regional language news paper about the date of the Board or its Sub Committee Meeting for audited yearly results (41)</td>
<td>(41)</td>
</tr>
<tr>
<td>30th June</td>
<td>Board Meeting to be held for approval of audited yearly results for companies adopting financial year Apr-Mar (41)</td>
<td>(41)</td>
</tr>
<tr>
<td>30th June</td>
<td>Audited yearly results to be published by the Company in at least one English daily news paper circulating in the whole or substantially whole of India and in one news paper published in the language of the region, where the registered office of the company is situated. (40)</td>
<td>(40)</td>
</tr>
<tr>
<td>July</td>
<td>A statement is required to be prepared by the company indicating the variations between projected utilization of funds and/or projected profitability statement made by the Company in its prospectus or letter of offer or object/s stated in the explanatory statement to the notice for the general meeting for considering preferential issue of securities, and the actual utilization of funds and/or actual profitability. (43)</td>
<td>(43)</td>
</tr>
<tr>
<td>July</td>
<td>Declaration from the Promoters in respect of their holding as on record date under SEBI (SAST) Regulations (40B)</td>
<td>(40B)</td>
</tr>
<tr>
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</tr>
<tr>
<td>July</td>
<td>Submission of yearly disclosure to the stock exchanges under SEBI (SAST) Regulations (40B)</td>
<td>On the record date for the purpose of dividend (Reg. 8 of SEBI (SAST) Regulations)</td>
</tr>
<tr>
<td>July</td>
<td>Despatch of Annual Report by the Company (31)</td>
<td>Six copies to each of the Stock Exchanges where the Company is listed and one copy each to all the recognized stock exchanges in India, as soon as it is issued to the shareholders</td>
</tr>
<tr>
<td>July</td>
<td>Certificate from either the auditors or practicing company secretaries regarding compliance of conditions of corporate governance to be obtained by the company and submitted [49(VII)(i)]</td>
<td>As part of the Annual Report and separately alongwith the Annual Report to be submitted to the Stock Exchange</td>
</tr>
<tr>
<td>July</td>
<td>Shareholders’/Investors’ Transfer/ Grievance Committee Meeting to be held by the Company (8, 41 &amp; 49)</td>
<td>Approval and processing of Transfer, Transmission, Demat and issue of Duplicate Share Certificate etc. to be placed before the Committee</td>
</tr>
<tr>
<td>July</td>
<td>Audit Committee Meeting for approving the Results of the Company to be held by the company (41 &amp; 49)</td>
<td>Approval of results is required for submission of the Results to the Board</td>
</tr>
<tr>
<td>15th July</td>
<td>Quarterly Compliance Report on Corporate Governance to be prepared by the company and signed by the Compliance Officer or Chief Executive Officer of the Company [49(VI)(ii)]</td>
<td>To be submitted to the Stock Exchange within 15 days from the end of each quarter</td>
</tr>
<tr>
<td>21st July</td>
<td>The Company is required to file the quarterly shareholding pattern in the revised format indicating therein the details of shares pledged or otherwise encumbered (35)</td>
<td>With the Stock Exchange within 21 days from the end of the quarter</td>
</tr>
<tr>
<td>23rd July</td>
<td>Notice of Board Meeting for unaudited quarterly results to be held by the Company (8, 41 &amp; 49)</td>
<td>To the Stock Exchange at least 7 days prior to the Board Meeting</td>
</tr>
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</tr>
<tr>
<td>23rd July</td>
<td>The Company is required to issue press release in at least one national news paper and one regional language news paper about the date of the Board or its Sub Committee Meeting for un-audited quarterly results (41)</td>
<td>At least 7 days prior to the Board Meeting</td>
</tr>
<tr>
<td>23rd July</td>
<td>Notice of Board Meeting to make additional quarterly disclosures as prescribed under Schedule VI of the Companies Act, 1956, is required to be sent where the company has not yet commenced its commercial production (41)</td>
<td>To the Stock Exchange at least 7 days prior to the Board Meeting</td>
</tr>
<tr>
<td>23rd July</td>
<td>The Company is required to issue press release in at least one national news paper and one regional language news paper about the date of the Board or its Sub Committee Meeting to make additional quarterly disclosures as prescribed under Schedule VI of the Companies Act, 1956. (41)</td>
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</tr>
<tr>
<td>30th July</td>
<td>Board Meeting to be held by the Company where the company has not yet commenced its commercial production, it will make additional quarterly disclosures as prescribed under Schedule VI of the Companies Act, 1956, for the balance of utilization of monies raised by issue and the form in which such utilization funds have been invested by the issuer. (41)</td>
<td>Board Meeting to be held within 1 month. Disclosures to be sent to the Stock Exchange</td>
</tr>
<tr>
<td>30th July</td>
<td>Intimation of quarterly results by the Company in the revised format along with segment wise revenue, results and capital employed (41)</td>
<td>To Stock Exchanges within 15 minutes from the closure of the Board Meeting</td>
</tr>
<tr>
<td>Date</td>
<td>Event</td>
<td>Details</td>
</tr>
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</tr>
<tr>
<td>1st August</td>
<td>Publication of quarterly results by the Company and statement of deviations in use of issue proceeds in at least one English daily newspaper circulating in the whole or substantially the whole of India and in one newspaper published in the language of the region, where the registered office of the company is situated.</td>
<td>Within 48 hours of the conclusion of the Board Meeting. Apart from the quarterly results, the statement of investor complaints and the statement of variation of utilization of funds are required to be published by the Company along with the quarterly results.</td>
</tr>
<tr>
<td></td>
<td>The Company is required to publish the number of investor complaints pending at the beginning of the quarter, received and disposed off during the quarter and lying unresolved at the end of the quarter (41)</td>
<td>For each of the years for which projections are provided in the prospectus/letter of offer/object/s stated in the explanatory statement to the notice for considering preferential issue of securities.</td>
</tr>
<tr>
<td></td>
<td>The Company is required to publish the statement of variation between projected utilization of funds and/or profitability statement made by it in its prospectus or letter of offer or object/s stated in the explanatory statement to the notice for the general meeting for considering preferential issue of securities, and the actual utilization of funds and/or actual profitability. (43)</td>
<td>Where there is a material variation, the company is required to furnish an explanation in the advertisement.</td>
</tr>
<tr>
<td>August</td>
<td>Shareholders’/Investors’ Transfer/ Grievance Committee Meeting to be held by the Company (8, 41 &amp; 49)</td>
<td>Approval and processing of Transfer, Transmission, Demat and issue of Duplicate Share Certificate etc. to be placed before the Committee.</td>
</tr>
<tr>
<td>31st August</td>
<td>Limited Review accompanied by a statement (approved by the Board of Directors) explaining the reasons to the Stock Exchanges, if in respect of any item given in the same proforma format varies by 10% or 10 lakhs whichever is higher from the respective unaudited quarterly.</td>
<td>To be submitted by the Company to the Stock Exchanges. This is not required if audited quarterly results are submitted within 1 month from the end of the third quarter.</td>
</tr>
<tr>
<td>Date</td>
<td>Event Description</td>
<td>Details</td>
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</tr>
<tr>
<td>September</td>
<td>Shareholders’/Investors’ Transfer/ Grievance Committee Meeting to be held by the Company (8, 41 &amp; 49)</td>
<td>Approval and processing of Transfer, Transmission, Demat and issue of Duplicate Share Certificate etc. to be placed before the Committee</td>
</tr>
<tr>
<td>October</td>
<td>Shareholders’/Investors’ Transfer/ Grievance Committee Meeting to be held by the Company (8, 41 &amp; 49)</td>
<td>Approval and processing of Transfer, Transmission, Demat and issue of Duplicate Share Certificate etc. to be placed before the Committee</td>
</tr>
<tr>
<td>October</td>
<td>A statement is required to be prepared by the company indicating the variations between projected utilization of funds and/or projected profitability statement made by the Company in its prospectus or letter of offer or object/s stated in the explanatory statement to the notice for the general meeting for considering preferential issue of securities, and the actual utilization of funds and/or actual profitability. (43)</td>
<td>Furnish on a quarterly basis to the Exchange for each of the years for which projections are provided in the prospectus/ letter of offer/object/s stated in the explanatory statement to the notice for considering preferential issue of securities</td>
</tr>
<tr>
<td>October</td>
<td>Audit Committee Meeting for approving the Results of the Company to be held by the company (41 &amp; 49)</td>
<td>Approval of results is required for submission of the Results to the Board</td>
</tr>
<tr>
<td>15th October</td>
<td>Quarterly Compliance Report on Corporate Governance to be prepared by the company and signed by the Compliance Officer or Chief Executive Officer of the Company [49(VI)(ii)]</td>
<td>To be submitted to the Stock Exchange within 15 days from the end of each quarter</td>
</tr>
<tr>
<td>21st October</td>
<td>The Company is required to file the quarterly shareholding pattern in the revised format indicating therein the details of the shares pledged or otherwise encumbered (35)</td>
<td>With the Stock Exchange within 21 days from the end of the quarter</td>
</tr>
<tr>
<td>Date</td>
<td>Event Description</td>
<td>Deadline</td>
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</tr>
<tr>
<td>23rd October</td>
<td>Notice of Board Meeting to make additional quarterly disclosures as prescribed under Schedule VI of the Companies Act, 1956, is required to be sent where the company has not yet commenced its commercial production.</td>
<td>To the Stock Exchange at least 7 days prior to the Board Meeting</td>
</tr>
<tr>
<td>23rd October</td>
<td>The Company is required to issue press release in at least one national newspaper and one regional language newspaper about the date of the Board or its Sub Committee Meeting to make additional quarterly disclosures as prescribed under Schedule VI of the Companies Act, 1956.</td>
<td>At least 7 days prior to the Board Meeting</td>
</tr>
<tr>
<td>23rd October</td>
<td>Notice of Board Meeting for unaudited quarterly results to be sent by the Company.</td>
<td>To the Stock Exchange at least 7 days prior to the Board Meeting</td>
</tr>
<tr>
<td>23rd October</td>
<td>The Company is required to issue press release in at least one national newspaper and one regional language newspaper about the date of the Board or its Sub Committee Meeting for unaudited quarterly results.</td>
<td>At least 7 days prior to the Board Meeting</td>
</tr>
<tr>
<td>30th October</td>
<td>Board Meeting to be held by the Company where the company has not yet commenced its commercial production, it will make additional quarterly disclosures as prescribed under Schedule VI of the Companies Act, 1956, for the balance of utilization of monies raised by issue and the form in which such utilization funds have been invested by the issuer.</td>
<td>Board Meeting to be held within 1 month. Disclosures to be sent to the Stock Exchange</td>
</tr>
<tr>
<td>30th October</td>
<td>Board Meeting for the Unaudited quarterly Results and</td>
<td>Within 1 month from the end of</td>
</tr>
<tr>
<td>Date</td>
<td>Event Description</td>
<td>Timeframe</td>
</tr>
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</tr>
<tr>
<td>30th October</td>
<td>Intimation of quarterly results by the Company in the revised format along with segment wise revenue, results and capital employed.</td>
<td>To Stock Exchanges within 15 minutes from the closure of the Board Meeting</td>
</tr>
<tr>
<td>30th October</td>
<td>The Company is required to give intimation that it will publish audited half yearly results within 2 months from the close of the half year.</td>
<td>In advance to the Stock Exchange</td>
</tr>
<tr>
<td>30th October</td>
<td>Submission of Half yearly Audit from a Practicing Company Secretary. This is required to be submitted to the Company by the Registrar &amp; Transfer Agent (RTA).</td>
<td>Within 1 month from the end of half year, to be submitted to the Exchange 24 hours of the receipt of the certificate by the Company</td>
</tr>
<tr>
<td>November</td>
<td>Shareholders'/Investors' Transfer/ Grievance Committee Meeting to be held by the Company.</td>
<td>Approval and processing of Transfer, Transmission, Demat and issue of Duplicate Share Certificate etc. to be placed before the Committee</td>
</tr>
<tr>
<td>1st November</td>
<td>Publication of quarterly results by the Company and statement of deviations in use of issue proceeds in at least one English daily newspaper circulating in the whole or substantially the whole of India and in one newspaper published in the language of the region, where the registered office of the company is situated. The Company is required to publish the number of investor complaints pending at the beginning of the quarter, received and disposed off during the quarter and lying unresolved at the end of the quarter.</td>
<td>Within 48 hours of the conclusion of the Board Meeting. Apart from the quarterly results, the statement of investor complaints and the statement of variation of utilization of funds are required to be published by the Company along with the quarterly results</td>
</tr>
<tr>
<td>30th October</td>
<td>The Company is required to provide quarter wise revenue, results and capital employed report to be held by the Company.</td>
<td>For each of the years for which</td>
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<tr>
<td>publish the statement of variation between projected utilization of funds and/or projected profitability statement made by it in its prospectus or letter of offer or object/s stated in the explanatory statement to the notice for the general meeting for considering preferential issue of securities, and the actual utilization of funds and/or actual profitability. (43)</td>
<td>projects are provided in the prospectus/letter of offer/object/s stated in the explanatory statement to the notice for considering preferential issue of securities Where there is a material variation, the company is required to furnish an explanation in the advertisement.</td>
<td>23rd November Notice of Board Meeting for audited half yearly results to be sent by the Company (41) To the Stock Exchange at least 7 days prior to the Board Meeting</td>
</tr>
<tr>
<td>23rd November The Company is required to issue press release in at least one national newspaper and one regional language newspaper about the date of the Board or its Sub Committee Meeting for audited half yearly results. (41)</td>
<td>At least 7 days prior to the Board Meeting</td>
<td></td>
</tr>
<tr>
<td>30th November Board Meeting to be held by the Company for approval of audited half yearly results for companies adopting financial year Apr-Mar (41)</td>
<td>Within 2 months from the end of the quarter Not required if the company submits unaudited 2nd quarter results</td>
<td>30th November Intimation of half yearly audited results by the Company (41) To Stock Exchanges within 15 minutes from the closure of the Board Meeting</td>
</tr>
<tr>
<td>30th November Limited Review accompanied by a statement (approved by the Board of Directors) explaining the reasons to the Stock Exchanges, if in respect of any item given in the same proforma format varies by 10% or 10 lakhs whichever is higher from the respective unaudited quarterly results as determined after the “Limited Review” by the Auditors (41)</td>
<td>To be submitted by the Company to the Stock Exchanges. This is not required if audited quarterly results are submitted within 1 month from the end of the third quarter</td>
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</tr>
<tr>
<td>December</td>
<td>Shareholders’/Investors’ Transfer/ Grievance Committee Meeting to be held by the Company (8, 41 &amp; 49)</td>
<td>Approval and processing of Transfer, Transmission, Demat and issue of Duplicate Share Certificate etc. to be placed before the Committee</td>
</tr>
<tr>
<td>2nd December</td>
<td>Publication of audited half yearly results by the Company in at least one English daily news paper circulating in the whole or substantially the whole of India and in one news paper published in the language of the region, where the registered office of the company is situated. The Company is required to publish the number of investor complaints pending at the beginning of the quarter, received and disposed off during the quarter and lying unresolved at the end of the quarter (41)</td>
<td>Within 48 hours of the conclusion of the Board Meeting. Apart from the audited half yearly results the statement of investor complaints and the statement of variation of utilization of funds are required to be published by the Company alongwith the half yearly audited results</td>
</tr>
<tr>
<td></td>
<td>The Company is required to publish the statement of variation between projected utilization of funds and/or projected profitability statement made by it in its prospectus or letter of offer or object/s stated in the explanatory statement to the notice for the general meeting for considering preferential issue of securities, and the actual utilization of funds and/or actual profitability. (43)</td>
<td>For each of the years for which projections are provided in the prospectus/ letter of offer/ object/s stated in the explanatory statement to the notice for considering preferential issue of securities Where there is a material variation, the company is required to furnish an explanation in the advertisement.</td>
</tr>
</tbody>
</table>

**ANNEXURE B**

**EVENT BASED COMPLIANCES**

<table>
<thead>
<tr>
<th>Clause No. of the Listing Agreement</th>
<th>Provisions of the Listing Agreement</th>
<th>Compliance requirements</th>
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<tbody>
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<tr>
<td><strong>13</strong></td>
<td>In case of any attachment or prohibitory orders restraining the Company from transferring securities out of the names of the registered holders, the Company is required to furnish to the Exchange particulars of the number of securities so affected, the distinctive numbers of such securities and the names of the registered holders thereof.</td>
<td>Promptly notify the Exchange</td>
</tr>
<tr>
<td><strong>16</strong></td>
<td>Where the company closes the transfer books for declaration of dividend or bonus shares or issue of shares for conversion of debentures or of shares arising out of rights attached to debentures</td>
<td>7 days advance notice required</td>
</tr>
<tr>
<td><strong>16</strong></td>
<td>The Company on whose stocks, derivatives are available or whose stocks form part of an index on which derivatives are available, notice of corporate actions like mergers, demergers, splits and bonus shares</td>
<td>Notice period of thirty days to Exchanges</td>
</tr>
<tr>
<td><strong>19(a)</strong></td>
<td>The Company is required to give prior intimation of the Board Meeting where Buyback of securities, declaration or recommendation of dividend or issue of convertible debentures or of debentures carrying a right to subscribe to equity shares or the passing over of dividend is due to be considered</td>
<td>2 days in advance intimation to the Stock Exchange</td>
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<td><strong>(3)</strong></td>
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<tr>
<td>(In case of NSE, prior intimation by the Company of the Board meeting where recommendation or declaration of dividend or a rights issue or convertible debentures or of debentures carrying a right to subscribe to equity shares or the passing over of the dividend is due to be considered. The company is required to recommend or declare all dividend and/or cash bonuses at least five days before commencement of the closure of its transfer books or the record date fixed for the purpose.)</td>
<td>To give notice simultaneously to the Stock Exchanges (No prior intimation to the Exchange is required about the Board Meeting in case the declaration of Bonus by the Company is not on the agenda of the Board Meeting)</td>
<td></td>
</tr>
<tr>
<td>19(b)</td>
<td>In case the proposal for declaration of bonus is communicated to the Board of Directors of the company as part of the agenda papers</td>
<td></td>
</tr>
<tr>
<td>19(c)</td>
<td>The company is required to recommend BSE or declare all dividend and/or cash bonuses</td>
<td>At least 5 days before commencement of the closure of its transfer books or the record date fixed for the purpose.</td>
</tr>
<tr>
<td>19(c)</td>
<td>The Issuers are also required to send the NSE information on corporate actions in the format which is given in Schedule IV by e-mail (<a href="mailto:cmlist@nse.co.in">cmlist@nse.co.in</a>)</td>
<td>Information to be sent to Stock Exchanges. No time limit specified.</td>
</tr>
<tr>
<td>19(d)</td>
<td>Proposal for Buyback of securities in any NSE Board Meeting</td>
<td>At least 7 days prior notice to Stock Exchange.</td>
</tr>
<tr>
<td>20</td>
<td>The Company will immediately on the date of the Board Meeting held to consider or decide the following: (a) all dividends and/or cash bonuses recommended or declared or the decision to pass any dividend or interest payment; (b) the total turnover, gross profit/</td>
<td>Intimate to the Exchange within 15 minutes of the closure of the Board Meetings by Letter/ fax (or, if the meeting be held outside the City of Mumbai, by fax/telegram)</td>
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</tr>
<tr>
<td>(1)</td>
<td>loss, provision for depreciation, tax provisions and net profits for the year (with comparison with the previous year) and the amounts appropriated from reserves, capital profits, accumulated profits of past years or other special source to provide wholly or partly for the dividend, even if this calls for qualification that such information is provisional or subject to audit.</td>
<td>(c) The decision on Buyback of Securities.</td>
</tr>
<tr>
<td>In case of NSE 20(c) above is 20(d) and 20(c)</td>
<td>The Issuers are also required to send the information on financial results by e-mail in the format which is given in Schedule V</td>
<td>The information is required to be sent by the company to the Stock Exchanges. No time limit specified.</td>
</tr>
<tr>
<td>21</td>
<td>The Company is required to notify the date on and from which the dividend on shares, interest on debentures and bonds, and redemption amount of redeemable shares or of debentures and bonds will be payable</td>
<td>Notify the Exchange at least 21 days in advance of the date</td>
</tr>
<tr>
<td>22</td>
<td>The Company will immediately on the date of the meeting of the Board of Directors held to consider or decide the following: (a) short particulars of any increase of capital whether by issue of bonus shares through capitalization, or by way of right shares to be offered to the shareholders or debenture holders, or in any other way; (b) short particulars of the reissue of forfeited shares or securities, or the issue of shares or securities held in</td>
<td>Intimate to the Exchange within 15 minutes of the closure of the Board Meetings by Letter/fax (or, if the meeting be held outside the City of Mumbai, by fax/telegram)</td>
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<td>reserve for future issue or the creation in any form or manner of new shares or securities or any other rights, privileges or benefits to subscribe to; (c) short particulars of any other alterations of capital, including calls; (d) any other information necessary to enable the holders of the listed securities of the Company to appraise its position and to avoid the establishment of a false market in such listed securities.</td>
<td>To be filed with the stock exchange for approval at least a month before it is presented to the Court or Tribunal.</td>
<td></td>
</tr>
<tr>
<td>24(f)</td>
<td>The Company is required to file any scheme/petition proposed to be filed before any Court or Tribunal under Sections 391, 394 and 101 of the Companies Act, 1956</td>
<td>To be filed with the stock exchange for approval at least a month before it is presented to the Court or Tribunal.</td>
</tr>
<tr>
<td>25</td>
<td>In the event of the Company granting any options to purchase any shares of the Company, the Company will notify the following— (a) of the number of shares covered by such options, of the terms thereof and of the time within which they may be exercised; (b) of any subsequent changes or cancellation or exercise of such options.</td>
<td>Promptly notify the Exchange</td>
</tr>
<tr>
<td>26</td>
<td>The Issuer will not select any of its listed securities for redemption otherwise than pro rata or by lot and will furnish any information requested in reference to such redemption.</td>
<td>Promptly furnish the Exchange</td>
</tr>
<tr>
<td>27</td>
<td>The Company will notify the following—</td>
<td>Promptly notify the Exchange</td>
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<tr>
<td>(a) any action which will result in the redemption, cancellation or retirement in whole or in part of any securities listed on the Exchange;</td>
<td></td>
<td>21 days’ prior notice to the Exchange of the proposed exchange and making an application for listing of the securities as changed if the Exchange shall so require.</td>
</tr>
<tr>
<td>(b) the intention to make a drawing of such securities, intimating at the same time the date of the drawing and the period of the closing of the Transfer Books (or the date of striking of the balance) for the drawing;</td>
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<tr>
<td>(c) the amount of security outstanding after any drawing has been made.</td>
<td></td>
<td></td>
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<tr>
<td>28</td>
<td>The Company is required to intimate the Exchange prior to making any change in the form or nature of any of its securities that are listed on the Exchange or in the rights or privileges of the holders thereof</td>
<td>Promptly notify the Exchange</td>
</tr>
<tr>
<td>29</td>
<td>The Company is required to notify any proposed change in the general character or nature of its business.</td>
<td></td>
</tr>
<tr>
<td>30</td>
<td>The Company will notify the following:</td>
<td>Promptly notify the Exchange</td>
</tr>
<tr>
<td></td>
<td>(a) any change in the Company’s directorate by death, resignation, removal or otherwise;</td>
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<td></td>
<td>(b) any change of Managing Director, Managing Agents or Securities and Treasures;</td>
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<td></td>
<td>(c) any change of Auditors appointed to audit the books and accounts of the Company</td>
<td></td>
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<tr>
<td>31</td>
<td>The Company is required to forward—</td>
<td>Forward promptly to the Exchange</td>
</tr>
<tr>
<td></td>
<td>(a) six copies of the Statutory and</td>
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</tbody>
</table>
Directors’ Annual Reports, Balance Sheets and Profits & Loss Accounts and of all periodical and special reports as soon as they are issued and one copy each to all the recognized stock exchanges in India;

(b) six copies of all notices, resolutions and circulars relating to new issue of capital prior to their dispatch to the shareholders;

(c) three copies of all the notices, call letters or any other circulars including notices of meetings convened u/s 391 or Section 394 read with Section 391 of the Companies Act, 1956 together with Annexures thereto, at the same time as they are sent to the shareholders, debenture holders or creditors or any class of them or advertised in the Press;

(d) copy of the proceedings at all Annual and Extraordinary General Meetings of the Company;

(e) three copies of all notices, circulars, etc., issued or advertised in the press either by the Company, or by any company which the Company proposes to absorb or with which the Company proposes to merge or amalgamate, or under orders of the court or any other statutory authority in connection with any merger, amalgamation, reconstruction, reduction of capital, scheme or arrangement, including notices, circulars, etc. issued or advertised in the press in
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<td>regard to meetings of shareholders or debenture holders or creditors or any class of them and copies of the proceedings at all such meetings.</td>
<td>No time limit specified</td>
<td></td>
</tr>
<tr>
<td>32</td>
<td>The Company is required to supply a copy of the complete and full Balance Sheet, Profit and Loss Account and the Directors' Report to each shareholder and upon application to any member of NSE.</td>
<td>No time limit specified</td>
</tr>
<tr>
<td>33</td>
<td>The Company is required to forward copies of all notices sent to its shareholders with respect to amendments to its Memorandum and Articles of Association and will file with the Exchange six copies (one of which will be certified) of such amendments.</td>
<td>Forward to the Exchange as soon as they shall have been adopted by the Company in general meeting.</td>
</tr>
<tr>
<td>34(g)</td>
<td>When the Company gives notice to its security holders by advertisement, it is required to advertise such notice in at least one leading National daily newspaper.</td>
<td>No time limit specified.</td>
</tr>
<tr>
<td>36</td>
<td>The Company will keep the Exchange informed of events such as strikes, lock-outs, closure on account of power cuts, etc.</td>
<td>The Exchange to be informed both at the time of occurrence of the event and subsequently after the cessation of the event.</td>
</tr>
<tr>
<td>36</td>
<td>The Company to keep the Exchange informed of all the events which will have bearing on the performance/operations of the company as well as price sensitive information</td>
<td>Immediately inform the Exchange</td>
</tr>
<tr>
<td>38(b)</td>
<td>The Company is required to pay the depositories Annual Custodial Fee at such rates as specified by SEBI from time to time</td>
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</tr>
<tr>
<td>47(a)</td>
<td>The Company is required to appoint a Compliance Officer</td>
<td>Inform as and when there is change in the Compliance Officer</td>
</tr>
<tr>
<td>47(e)</td>
<td>The Company is required to appoint Registrar &amp; Transfer Agents (RTA)</td>
<td>Inform if there is any change along with the MOU signed with RTA</td>
</tr>
<tr>
<td>47(e)</td>
<td>Copies of Memorandum of Understanding entered into with the RTA setting out their mutual responsibilities</td>
<td>Within 48 hours of entering into the agreement</td>
</tr>
<tr>
<td>51</td>
<td>File the following information, statements and reports on the Electronic Data Information Filing and Retrieval (EDIFAR) website maintained by National Information Centre (NIC), on-line, in such manner and format and within such time as may be specified by SEBI: 1. Full version of annual report including the balance sheet, profit and loss account, director’s report and auditor’s report; cash flow statements; half yearly financial statements and quarterly financial statements. 2. Corporate governance report. 3. Shareholding pattern statement. 4. Statement of action taken against the company by any regulatory agency. 5. Such other statement, information or report as may be specified by SEBI from time to time in this regard.</td>
<td>File the statements with the Exchange. No time limit specified in the Listing Agreement.</td>
</tr>
</tbody>
</table>

**ANNEXURE C**

**MONTHWISE COMPLIANCE CHECK LIST FOR A LISTED COMPANY**

<table>
<thead>
<tr>
<th>Month</th>
<th>Target Date</th>
<th>Matter</th>
<th>Remarks</th>
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</tr>
<tr>
<td>January</td>
<td>Shareholders’/Investors’ Transfer/Grievance Committee Meeting</td>
<td>Approval and process of Transfer, Transmission, Demat, Issue of Duplicate Share Certificate etc.</td>
<td></td>
</tr>
<tr>
<td>15th January</td>
<td>Submission of quarterly shareholding pattern</td>
<td>Within 15 days from the end of the quarter</td>
<td></td>
</tr>
<tr>
<td>January</td>
<td>Audit Committee Meeting for approving the Results of the Company</td>
<td>For submission of the Results to the Board</td>
<td></td>
</tr>
<tr>
<td>3rd or 4th week of January</td>
<td>Board Meeting for the Unaudited quarterly Results.</td>
<td>At least 7 days prior intimation to Stock Exchanges.</td>
<td></td>
</tr>
<tr>
<td>January</td>
<td>Intimation of quarterly results to Stock Exchanges</td>
<td>Within 15 minutes from the closure of the Board Meeting</td>
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<tr>
<td>January</td>
<td>Publication of quarterly results in newspapers</td>
<td>Within 48 hours of the conclusion of the Board Meeting</td>
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<tr>
<td>January</td>
<td>Submission of Limited Audit Review to Stock Exchanges</td>
<td>Within 2 months from the end of the quarter</td>
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<tr>
<td>January</td>
<td>Submission of Secretarial Audit to Stock Exchanges for the quarter</td>
<td>Within 30 days from the end of the quarter</td>
<td></td>
</tr>
<tr>
<td>February</td>
<td>Shareholders’/Investors’ Transfer/Grievance Committee Meeting</td>
<td>Approval and processing of Transfer, Transmission, Demat, Issue of Duplicate Share Certificates etc.</td>
<td></td>
</tr>
<tr>
<td>1st March</td>
<td>Disclosure of Interest</td>
<td>Form 24AA to be sent to all Directors for renewal of notice for General disclosure of interest.</td>
<td></td>
</tr>
<tr>
<td>1st March</td>
<td>Declaration under Section 274(1)(g) of the Companies Act, 1956</td>
<td>Format to be sent to all Directors for their declaration</td>
<td></td>
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<tr>
<td>March</td>
<td>Shareholders’/Investors’ Transfer/Grievance Committee Meeting</td>
<td>Approval and processing of Transfer, Transmission, Demat, Issue of Duplicate Share Certificates etc.</td>
<td></td>
</tr>
<tr>
<td>1st April</td>
<td>Sitting Fee Certificates</td>
<td>Issue certificates to Directors regarding payment of sitting fee.</td>
<td></td>
</tr>
<tr>
<td>1st April</td>
<td>Listing Fee</td>
<td>Listing fee to be paid for renewal.</td>
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</tr>
<tr>
<td>April</td>
<td>Shareholders’/Investors’ Transfer/Grievance Committee Meeting</td>
<td>Approval and processing of Transfer, Transmission, Demat, Issue of Duplicate Share Certificates etc.</td>
<td></td>
</tr>
<tr>
<td>15th April</td>
<td>Reconciliation</td>
<td>Reconciliation of Int./Dividend/Redemption/Conversion of Warrants/Call Money etc.</td>
<td></td>
</tr>
<tr>
<td>15th April</td>
<td>Submission of quarterly shareholding pattern</td>
<td>Within 15 days from the end of the quarter</td>
<td></td>
</tr>
<tr>
<td>21st April</td>
<td>Declaration from the Promoters in respect of their holding as on 31st March under SEBI Takeover Code</td>
<td>To be given to the Company within 21 days from the end of financial year</td>
<td></td>
</tr>
<tr>
<td>30th April</td>
<td>Submission of yearly disclosure to the stock exchanges under SEBI Takeover Code</td>
<td>Within 30 days from the end of the financial year</td>
<td></td>
</tr>
<tr>
<td>April</td>
<td>Submission of Half yearly Audit from a Practicing Company Secretary</td>
<td>Within 1 month from the end of half year</td>
<td></td>
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<tr>
<td>April</td>
<td>Submission of Secretarial Audit to Stock Exchanges for the quarter</td>
<td>Within 30 days from the end of the quarter</td>
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</tr>
<tr>
<td>May</td>
<td>Shareholders’/Investors’ Transfer/Grievance Committee Meeting</td>
<td>Approval and processing of Transfer, Transmission, Demat, Issue of Duplicate Share Certificates etc.</td>
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<tr>
<td>May</td>
<td>Audit Committee Meeting for approving the Results of the Company</td>
<td>For submission of the Results to the Board</td>
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<tr>
<td>May</td>
<td>Remuneration Committee Meeting for recommending the remuneration of MD &amp; Whole time Directors</td>
<td>For recommending to the Board</td>
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</tbody>
</table>
| 3rd or 4th week of May | Board Meeting for approving the Audited Results, Declaration of Dividend, Appointment of Auditors                                                                                                 | — At least 7 days prior intimation to the Stock Exchanges.  
— Publication of Audited Results for year within 3 months from the end of the year.  
— Get consent from auditors to act as Auditors for the year. |
<p>| May      | Cost Auditors                                                                                                                                         | Get consent from Cost Auditors, where applicable to act as Cost Auditor for the year and file application to the Central Government.                                                              |
| June     | Shareholders’/Investors’ Transfer Grievance Committee Meeting                                                                                                                                          | Approval and processing of Transfer, Transmission, Demat, Issue of Duplicate Share Certificates etc.                                                                                               |
| June     | Printing of Annual Report/Art Work                                                                                                                                                                | To decide Printing of Annual Report/Art Work                                                                                                                                                        |
| June     | Booking of hall for AGM                                                                                                                                         | Advance Booking of Hall for conducting AGM                                                                                                                                                         |
| July     | Publishing in news papers regarding Book Closure Dates                                                                                                                                               | At least 7 days prior to start of Book Closure                                                                                                                                                      |
| July     | Declaration from the Promoters in respect of their holding as on record date under SEBI Takeover Code                                                                                                  | To be given to the Company within 21 days from the record date for the purpose of dividend.                                                                                                           |
| July     | Submission of yearly disclosure                                                                                                                                                                      | Within 30 days from the record                                                                                                                                                                       |</p>
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<tbody>
<tr>
<td>to the stock exchanges under SEBI Takeover Code</td>
<td>date for the purpose of dividend</td>
<td></td>
</tr>
<tr>
<td>July</td>
<td>Fund Arrangement</td>
<td>Letter to Accounts for arrangement of funds for payment of Dividend.</td>
</tr>
<tr>
<td>July</td>
<td>Arrangement for AGM</td>
<td>All work relating to AGM including Chairman’s Speech etc. to be arranged.</td>
</tr>
<tr>
<td>July</td>
<td>Printing of Balance Sheet/Annual Report</td>
<td>To coordinate with various Departments.</td>
</tr>
<tr>
<td>July</td>
<td>Despatch of Annual Report</td>
<td>Despatch of Annual Report to shareholders/ Stock Exchanges etc.</td>
</tr>
<tr>
<td>July</td>
<td>Shareholders’/Investors’ Transfer/Grievance Committee Meeting</td>
<td>All transfers received upto the date of meeting is be included</td>
</tr>
<tr>
<td>15th July</td>
<td>Submission of quarterly shareholding pattern</td>
<td>Within 15 days from the end of the quarter</td>
</tr>
<tr>
<td>July</td>
<td>AGM</td>
<td>To hold Annual General Meeting</td>
</tr>
<tr>
<td>July</td>
<td>Audit Committee Meeting for quarterly un-audited results of the Company</td>
<td>For submission of the Results to the Board</td>
</tr>
<tr>
<td>3rd or 4th week of July (along-with AGM)</td>
<td>Board Meeting for the Un-audited Results for the Quarter</td>
<td>At least 7 days prior intimation to Stock Exchanges</td>
</tr>
<tr>
<td>July</td>
<td>Intimation of quarterly results to Stock Exchanges</td>
<td>Within 15 minutes from the closure of the Board Meeting</td>
</tr>
<tr>
<td>July</td>
<td>Publication of quarterly results in newspapers</td>
<td>Within 48 hours of the conclusion of the Board Meeting</td>
</tr>
<tr>
<td>July</td>
<td>Payment of Commission</td>
<td>Sent letter to Accounts for payment of commission to Directors for the financial year</td>
</tr>
<tr>
<td>July</td>
<td>Draft of Dividend Warrant</td>
<td>Approve draft of Dividend Warrant</td>
</tr>
<tr>
<td>July</td>
<td>Printing &amp; Despatch (Intt./)</td>
<td>Arrange to print warrants/</td>
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<tr>
<td>Dividend</td>
<td>dispatch</td>
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<tr>
<td>July</td>
<td>Submission of Limited Audit Review to Stock Exchanges</td>
<td>Within 2 months from the end of the quarter</td>
</tr>
<tr>
<td>July</td>
<td>Submission of Secretarial Audit to Stock Exchanges for the quarter</td>
<td>Within 30 days from the end of the quarter</td>
</tr>
<tr>
<td>August</td>
<td>Shareholders’/Investors’ Transfer/Grievance Committee Meeting</td>
<td>All transfers received upto the date of meeting to be included</td>
</tr>
<tr>
<td>August</td>
<td>Filing of Balance Sheet, Forms and Resolutions etc. with ROC</td>
<td>Within 30 days from the AGM</td>
</tr>
<tr>
<td>Sept.</td>
<td>Annual Return</td>
<td>Filing of Annual Return with concerned ROC (within 60 days of AGM)</td>
</tr>
<tr>
<td>Sept.</td>
<td>Shareholders’/Investors’ Transfer/Grievance Committee Meeting</td>
<td>Approval and processing of Transfer, Transmission, Demat, Issue of Duplicate Share Certificates etc.</td>
</tr>
<tr>
<td>October</td>
<td>Shareholders’/Investors’ Transfer/Grievance Committee Meeting</td>
<td>Approval and processing of Transfer, Transmission, Demat, Issue of Duplicate Share Certificates etc.</td>
</tr>
<tr>
<td>15th October</td>
<td>Submission of quarterly shareholding pattern</td>
<td>Within 15 days from the end of the quarter</td>
</tr>
<tr>
<td>October</td>
<td>Audit Committee Meeting for approving the Results of the Company</td>
<td>For submission of the Results to the Board</td>
</tr>
<tr>
<td>3rd or 4th week of October</td>
<td>Board Meeting for the Unaudited quarterly &amp; half yearly Results.</td>
<td>At least 7 days prior intimation to Stock Exchanges</td>
</tr>
<tr>
<td>October</td>
<td>Intimation of quarterly results to Stock Exchanges</td>
<td>Within 15 minutes from the closure of the Board Meeting</td>
</tr>
<tr>
<td>October</td>
<td>Publication of quarterly &amp; half yearly results in news papers</td>
<td>Within 48 hours of the conclusion of the Board Meeting</td>
</tr>
<tr>
<td>October</td>
<td>Submission of Limited Audit Review to Stock Exchanges</td>
<td>Within 2 months from the end of the quarter</td>
</tr>
</tbody>
</table>
30th October  Submission of yearly disclosure to the stock exchanges under SEBI Takeover Code

October  Submission of Secretarial Audit to Stock Exchanges for the quarter

Nov.  Shareholders'/Investors' Transfer/Grievance Committee Meeting

Nov.  Compliance status of Affiliate companies

Dec.  Shareholders'/Investors' Transfer/Grievance Committee Meeting

Dec.  Compliance status of Affiliate companies

**LESSON ROUND-UP**

- The listing of securities with the stock exchanges is ensured by way of entering into a listing agreement between the stock exchange where the securities are proposed to be listed and the issuing company.
- The process of listing includes initial listing, final listing, enlisting of securities openly for trading and continuous listing (i.e. to remain listed).
- Any listed company is required to comply with the provisions of listing agreement which are time based/event based.
- The Company is required to appoint the Company Secretary to act as Compliance Officer under clause 47(a) of the listing agreement.
- The listing agreement includes compliances pertaining to intimations to stock exchanges, publication of financial results, shareholding pattern, corporate governance matters, allotment, refund, share transfer related matters, etc.

**SELF-TEST QUESTIONS**

*(These are meant for recapitulation only. Answers to these questions are not to*
1. Briefly explain the points to be checked relating to publication of financial results.
2. Describe various times based recurring compliances under listing agreement.
3. What are the listing requirements under clause 49 of the listing agreement?
4. What are the various intimations/submissions which are to be made to the stock exchange?
STUDY VI
INTERNAL AUDIT OF DEPOSITORY PARTICIPANTS

LEARNING OBJECTIVES

The objective of this study lesson is to enable the students to understand

- An overview of Depository System
- Legal framework for Depository Participants
- Role of Depository Participants
- Objective and scope of Internal Audit of Depository Participants
- Check list on Internal Audit of Depository Participants

DEPOSITORY SYSTEM - AN OVERVIEW

The Depository System functions very much like the banking system. A bank holds funds in accounts whereas a Depository holds securities in accounts for its clients. A Bank transfers funds between accounts whereas a Depository transfers securities between accounts. In both systems, the transfer of funds or securities happens without the actual handling of funds or securities. Both the Banks and the Depository are accountable for the safe keeping of funds and securities respectively.

In the depository system, share certificates belonging to the investors are to be dematerialised and their names are required to be entered in the records of depository as beneficial owners. Consequent to these changes, the investors’ names in the companies’ register are replaced by the name of depository as the registered owner of the securities. The depository, however, does not have any voting rights or other economic rights in respect of the shares as a registered owner. The beneficial owner continues to enjoy all the rights and benefits and is subject to all the liabilities in respect of the securities held by a depository. Shares in the depository mode are fungible and cease to have distinctive numbers. The transfer of ownership changes in the depository is done automatically on the basis of delivery v. payment.

In the Depository mode, corporate actions such as IPOs, rights, conversions, bonus, mergers/amalgamations, subdivisions & consolidations are carried out without the movement of papers, saving both cost & time. Information of beneficiary owners is readily available. The issuer gets information on changes in shareholding pattern on a regular basis, which enables the issuer to efficiently monitor the changes in shareholdings.

The Depository system links the issuing corporates, Depository Participants (DPs), the Depositories and clearing corporation/ clearing house of stock exchanges. This network facilitates holding of securities in the soft form and effects transfers by means of account transfers.

Depository Participant

Just as a brokers act an agent of the investor at the Stock Exchange; a Depository Participant (DP) is the representative (agent) of the investor in the depository system providing the link between the Company and investor through the
Depository. The Depository Participant maintains securities account balances and
intimate the status of holding to the account holder from time to time. According to
SEBI guidelines, Financial Institutions like banks, custodians, stockbrokers etc. can
become participants in the depository. A DP is one with whom an investor needs to
open an account to deal in shares in electronic form. While the Depository can be
compared to a Bank, DP is like a branch of that bank with which an account can be
opened. The main characteristics of a depository participant are as under:

— Acts as an Agent of Depository
— Customer interface of Depository
— Functions like Securities Bank
— Account opening
— Facilitates dematerialisation
— Instant transfer on pay-out
— Credits to investor in IPO, rights, bonus
— Settles trades in electronic segment

LEGAL FRAMEWORK FOR DEPOSITORY PARTICIPANTS

The legal framework for a depository system has been laid down by the
Depositories Act, 1996 and is regulated by SEBI. The depository business in India is
regulated by—

— The Depositories Act, 1996
— The SEBI (Depositories and Participants) Regulations, 1996
— Bye-laws of Depository
— Business Rules of Depository.

Apart from the above, Depositories and Depository participants are also
governed by certain provisions of:

— The Companies Act, 1956
— The Indian Stamp Act, 1899
— Securities and Exchange Board of India Act, 1992
— Securities Contracts (Regulation) Act, 1956
— Benami Transaction (Prohibition) Act, 1988
— Income Tax Act, 1961
— Bankers’ Books Evidence Act, 1891

The legal framework for depository system as envisaged in the Depositories Act,
1996 provides for the establishment of single or multiple depositories. Any body to be
eligible for providing depository services must be formed and registered as a
company under the Companies Act, 1956 and seek registration with SEBI and obtain
a Certificate of Commencement of Business from SEBI on fulfillment of the
prescribed conditions. The investors opting to join depository mode are required to
enter into an agreement with depository through a participant who acts as an agent of depository. The agencies such as custodians, banks, financial institutions, large corporate brokerage firms, non-banking financial companies etc. act as participants of depositaries. The companies issuing securities are also required to enter into an agreement with the Depository.

ROLE OF DEPOSITORY PARTICIPANTS (DPs)

A depository interfaces with market participants e.g. Brokers, clearing members and investors through its agents called Depository Participants (DP). Any person wanting to avail the services of depository has to enter into an agreement with the depository participant acting as an against of depository. We shall restrict our analysis on the functioning of the Depository system to the functioning, role and ultimately the audit of DPs. The role of DP can be best analysed by placing a reference on the following:

(i) The Depositories Act, 1996;
(ii) The SEBI (Depositories and Participants) Regulations, 1996;
(iii) The Byelaws of the Depository;
(iv) The Business Rules of the Depository; and
(v) The terms and conditions of Agreements to which the DP is a party.

Under the Depositories Act, 1996:

(i) Section 2(1)(g) of the Depositories Act, 1996 defines a participant to mean a person registered under Sub-section (1A) of section 12 of the SEBI Act, 1992. Section 12(1A) of the SEBI Act, 1992 provides that no DP shall buy or sell or deal in securities except under and in accordance with the conditions of a certificate of registration granted by SEBI in accordance with the regulations made by SEBI.

(ii) Section 4 provides that a Depository shall enter into an agreement with one or more DPs as its agents and such an agreement shall be in such form as specified by the bye-laws of the Depository.

(iii) Section 5 provides that any person may avail of Depository services by executing an agreement through a DP with the Depository.

(iv) Section 7(1) provides that every Depository shall on receipt of intimation from a DP, register the transfer of security in the name of transferee.

(v) Section 16 provides that in event of any loss being caused to the beneficial owner by the negligence of the Depository or the DP, the Depository shall in the first place indemnify the beneficial owner and where the loss has been caused by the DP, the Depository shall recover the loss from it.

(vi) Section 18 – The DP can be called upon by the SEBI to furnish such information relating to the securities held in a depository as may be required. Also its affairs can be inspected by any person so authorized by SEBI.

(vii) Section 19A to 19G – Under these sections a DP is liable to penalty for failure to furnish information/return; enter into agreements; redress Investors’ grievances; make delay in dematerialisation or issue of certificates of
Under the SEBI (Depositories and Participants) Regulations, 1996

(i) Regulation 6A stipulates that the DPs shall be subject to compliance with SEBI (criteria for Fit and Proper Person) Regulation, 2004.

(ii) Regulations 16 and 17 deal with registration of DPs. It is stipulated that an application for grant of a certificate of registration shall be made to SEBI in form E through each Depository in which the applicant proposes to act as a participant accompanied by the prescribed fees. The Depository shall forward the application to SEBI not later than 30 days along with its recommendations and certifying that the applicant complies with the eligibility criteria including adequate infrastructure as provided for in these regulations and the bye-laws of the depository. Regulation 18 provides for furnishing of further information, clarifications to SEBI or personal attendance of the applicant or the depository to which the applicant is to be admitted as a participant.

(iii) Regulation 19 stipulates the categories of entities which are eligible for being registered as DPs viz. Banks, Financial Institutions, Stock Brokers etc.

For the purpose of grant of certificate of registration, the Board shall take into account all matters which are relevant to or relating to the efficient and orderly functioning of a participant and in particular, whether the applicant complies with the following requirements, namely:

(a) the applicant belongs to one of the following categories,-

   (i) a public financial institution as defined in Section 4A of the Companies Act, 1956 (1 of 1956);

   (ii) a bank included for the time being in the Second Schedule to the Reserve Bank of India Act, 1934 (2 of 1934);

   (iii) a foreign bank operating in India with the approval of the Reserve Bank of India;

   (iv) a State Financial Corporation established under the provisions of Section 3 of the State Financial Corporations Act, 1951 (63 of 1951);

   (v) an institution engaged in providing financial services, promoted by any of the institutions mentioned in sub-clause (i), (ii), (iii), (iv) jointly or severally;

   (vi) a custodian of securities who has been granted a certificate of registration by the Board under Sub-section (1A) of Section 12 of the Act;

   (vii) a clearing corporation or a clearing house of a stock exchange;

   (viii) a stock broker who has been granted a certificate of registration by the Board under Sub-section (1) of Section 12 of the Act:

Provided that the stock-broker shall have a minimum net worth of rupees 50 lakhs and the aggregate value of the portfolio of securities of the beneficial owners held in dematerialised form in a depository through him, shall not exceed 100 times of the net worth of the stock
broker.

Provided further that if the stock broker seeks to act as a participant in more than one depository, he shall comply with the criteria specified in the first proviso separately for each such depository; or

Provided further that where the stockbroker has a minimum networth of Rupees Ten crore, the limits on the aggregate value of the portfolio of securities of the beneficial owners held in dematerialized form in a depository through him shall not be applicable.

(ix) a non-banking finance company, having a net worth of not less than rupees fifty lakhs:

Provided that such company shall act as a participant only on behalf of itself and not on behalf of any other person;

Provided further that a non-banking finance company may act as a participant on behalf of any other person, if it has a networth of Rs. 50 crores in addition to the networth specified by any other authority]

(x) a registrar to an issue or share transfer agent who has a minimum net worth of rupees ten crores and who has been granted a certificate of registration by the Board under Sub-section (1) of Section 12 of the Act.

(b) the applicant is eligible to be admitted as a participant of the depository through which it has made the application to the Board;

(c) the applicant has adequate infrastructure, systems, safeguards and trained staff to carry on activity as a participant; and

(cc) the applicant is a fit and proper person.

(d) the grant of certificate of registration is in the interests of investors in the securities market.

(iv) Regulation 20 stipulates that the certificate of registration as a DP shall be granted by SEBI in Form F. The grant of this certificate shall be subject to the following conditions:

— The DP shall pay the prescribed registration fee within 15 days of receipt of intimation from the SEBI specified in Part A of the Second Schedule, in the manner specified in Part B. The DP shall also pay Annual fees specified in part A of the Second Schedule in the manner specified in Part B thereof.

— The DP shall comply with the provisions of the SEBI Act 1992, the Depositories Act 1996, the Bye-laws of the Depository, agreements and these Regulations.

— The DP shall redress the grievances of the beneficial owners within 30 days of the date of the receipt of the complaint and keep the Depository informed about the number and the nature of redressal.

Also, the depository through which an application for certificate of registration has been forwarded, should hold a certificate of commencement of business under Regulation 14. If any information previously submitted by the participant to the SEBI is found to be false or
misleading in any material particular or if there is any change in such information participant shall forthwith inform the SEBI in writing.

(v) Regulation 20A provides that a DP, shall abide by the code of conduct as specified in the third schedule.

(vi) Regulation 21 stipulates that the certificate of registration shall be valid for a period of 5 years from the date of its issue or renewal.

(vii) Regulation 22 stipulates that 3 months before the expiry of the period of validity of a certificate, the DP shall (if it so desires) make an application for renewal in Form E through the Depository in which he is a participant in the same manner as if it were a fresh application for registration.

(viii) Regulations 23 and 24 provide that if the application for registration under regulation 16 or 19, has been rejected the DP should cease to carry on any activity as such unless, SEBI has, in the interest of investors in the securities market permitted the DP to carry on its activities undertaken prior to the receipt of intimation of refusal.

(ix) Regulation 41 provides that every DP shall enter into an agreement as a participant on his behalf in the manner specified by the Depository in its Byelaws.

(x) Regulation 42 provides that:

— Separate accounts shall be opened by every DP in the name of each of the beneficial owners and the securities of each beneficial owner shall be segregated and shall not be mixed up with the securities of other beneficial owners or with the participant’s own securities.

— The DP shall register the transfer of securities to or from a beneficial owner’s account only on receipt of instructions from the beneficial owner and thereafter confirm the same to the beneficial owner in a manner specified by the Byelaws of the Depository.

— Every entry in the beneficial owner’s account shall be supported by electronic instructions or any other mode of instruction received from the beneficial owner in accordance with the agreement with the beneficial owner.

(xi) Regulation 43 provides that every DP shall provide statements of account to the beneficial owner in such form and in such manner and at such time as provided in the agreement with the beneficial owner.

(xii) Regulation 44 provides that every DP shall allow a beneficial owner to withdraw or transfer from his account in such manner as specified in the agreement with the beneficial owner. Also, according to Regulation 33, every depository can allow any participant to withdraw or transfer its account, if the request for such withdrawal or transfer is in accordance with stipulated conditions.

(xiii) Regulation 45 provides that every DP shall maintain continuous electronic means of communication with the Depository.

(xiv) Regulation 47 provides that every DP shall reconcile its records with every Depository in which it is a participant on a daily basis.
(xv) Regulation 48 provides that every DP shall submit periodic returns to SEBI and to the Depository in the format specified by SEBI or the Byelaws of the Depository.

(xvi) Regulation 49 provides that every DP shall maintain the following records and documents:
(a) records of all the transactions entered into with a depository and with a beneficial owner;
(b) details of security dematerialised, rematerialised on behalf of beneficial owners with whom it has entered into an agreement;
(c) records of instructions received from beneficial owners and statements of account provided to beneficial owners; and
(d) records of approval, notice, entry and cancellation of pledge or hypothecation, as the case may be.

Further, the DP shall intimate SEBI about the place where the records and documents are maintained. It shall make available for the inspection of the depository in which it is participant. The DP shall preserve records and documents for a minimum period of 5 years.

(xvii) Regulation 50 provides that where records are kept electronically by a DP, it shall ensure that the integrity of the data processing systems is maintained at all times and take all precautions necessary to ensure that the records are not lost, destroyed or tampered with and in the event of loss or destruction, ensure that sufficient back up of records is available at all times at a different place.

(xviii) Regulation 51 stipulates that if a DP enters into an agreement with more than one depository, it shall maintain records specified in Regulation 49 separately in respect of each depository.

(xix) Regulation 52 provides that a DP shall not assign or delegate its functions to any other person without the prior approval of the Depository.

(xx) Regulation 53B provides that the grievances of the beneficial owners shall be redressed within thirty days of receipt of complaint and the depository shall be informed about the number and nature of grievances redressed and remaining pending.

(xxii) Regulation 54 provides that:

1. Any beneficial owner, who has entered into an agreement with a DP, shall inform the DP of the details of the certificate of security which is to be dematerialised, and shall surrender such certificate to the DP;
   Provided that where a beneficial owner has appointed a custodian of securities, then he may surrender the certificates of security to the DP through his custodian of securities.

2. The DP shall, on receipt of information under sub-regulation (1), forward such details of the certificate of security to the depository and shall confirm to the depository that an agreement has been entered into between the DP and the beneficial owner.
(3) The DP shall maintain records indicating the names of beneficial owners of the securities surrendered, the number of securities and other details of the certificate of security received.

(4) The DP shall within seven days of receipt of security certificate furnish to the issuer, details specified in sub-regulation (2) along with the certificate of security referred to in sub-regulation (1).

(xxii) Regulation 58 provides that:

(1) If a beneficial owner intends to create a pledge on a security owned by him, he shall make an application to the depository through the DP who has his account in respect of such securities.

(2) The DP after satisfaction that the securities are available for pledge shall make a note in its records of the notice of pledge and forward the application to the depository.

(3) The depository after confirmation from the pledgee that the securities are available for pledge with the pledger shall within fifteen days of the receipt of the application create and record the pledge and send an intimation of the same to the DPs of the pledger and the pledgee.

(4) On receipt of the intimation under sub-regulation (3) the DPs of both the pledgor and the pledgee, shall inform the pledgor and the pledgee respectively of the entry of creation of the pledge.

(5) If the depository does not create the pledge, it shall send along with the reasons as intimation to the DPs of the pledger and the pledgee.

(6) The entry of pledge made under sub-regulation (3) may be cancelled by the depository if pledger or the pledgee makes an application to the depository through its DP:

Provided that no entry of pledge shall be cancelled by the depository without prior concurrence of the pledgee.

(7) The depository on the cancellation of the entry of pledge shall inform the DP of the pledger.

(8) Subject to the provisions of the pledge document, the pledgee may invoke the pledge and on such invocation, the depository shall register the pledgee as beneficial owner of such securities and amend its records accordingly.

(9) After amending its records under sub-regulation (8) the depository shall immediately inform the DPs of the pledger and pledgee of the change who in turn shall make the necessary changes in their records and inform the pledger and pledgee, respectively.

(10) (a) If a beneficial owner intends to create a hypothecation on a security owned by him he may do so in accordance with the provisions of sub-regulations (1) to (9).

(b) The provisions of sub-regulations (1) to (9) shall mutatis mutandis
apply in such cases of hypothecation:

Provided that the depository before registering the hypothecation as a beneficial owner shall obtain the prior concurrence of the hypothecator.

(11) No transfer of security in respect of which a notice or entry of pledge or hypothecation is in force shall be effected by a DP without the concurrence of the pledgee or the hypothecatee as the case may be.

According to Regulation 58A, a depository or a participant or any of their employees shall not render, directly or indirectly, any investment advice about any security in the publicly accessible media, whether real time or non-real time, unless a disclosure of his interest including long or short position in the said security has been made, while rendering such advice. In case, an employee of the depository or the participant is rendering such advice, he shall also, disclose the interest of his dependent family members and the employer including their long or short position in the said security, while rendering such advice.

The operations and procedures other than trading involving the Depository and its other business partners could be summarised as under:

(a) Dematerialisation;
(b) Rematerialisation;
(c) Corporate Actions/Benefits; and
(d) Pledge/Hypothecation.

DEMATeRIALISATION

Dematerialisation is a process of conversion of physical certificates into electronic balances. Before the process of dematerialisation is set in motion some essential prerequisites need to be considered as under:

(a) An investor must open an Account with a DP.
(b) Only the securities eligible for demat can be dematerialised.
(c) The securities must be in the name of the account holder and owned by him.
(d) A separate demat requisition form (DRF) is required for each issuer.
(e) A separate DRF is required for lock-in and lockfree securities.
(f) The DRF form must be signed by all the joint holders.

REMatERIALISATION

Rematerialisation means the conversion of dematerialised holdings back into the physical certificates.

In a simplified form the process of Rematerialisation could be explained hereunder:

(a) Investor to submit the Rematerialisation Request Form (RRF) to the DP.
(b) DP to electronically intimate the Depository.
(c) DP to submit RRF to the Registrar/Issuer Company.

(d) Depository confirms rematerialisation request to the Registrar/Issuer Company.

(e) Registrar/Issuer Company verifies particulars, prints certificates and intimates the Depository.

(f) Depository updates Accounts and downloads details to DP.

(g) Registrar/Issuer despatches certificates to the investor.

Corporate actions are benefits given by a company to its members. Corporate benefits/actions would include rights issues/bonus issues, dividend payments, interest payments etc. [i.e. both monetary and non-monetary benefits].

Whenever a corporate action is announced, the issuer or its registrar and transfer agent, should inform its depository just after the day of communication of the same to the relevant stock exchange(s). The depository should then inform the participants, through a circular about the relevant action, the no-delivery period, the cut-off date and the procedure to be followed by the participants. The participants, upon receiving such information, should ensure that:

(i) the changes in tax status, bank details, change of address etc in the beneficial owner’s accounts are updated in advance of the book closure record date.

(ii) all positions in the transitory accounts e.g. Clearing accounts and intermediary accounts are cleared and balances lying therein are transferred to the relevant beneficiary accounts in advance of the book closure/relevant dates.

(iii) while transferring securities to the clearing accounts, only the settlement number in which the securities will ultimately be settled is mentioned, rather than the settlement number in respect of which there is no-delivery.

(iv) it remains connected till end-of-day processing on the record date or the business date immediately prior to book closure.

On the basis of the particulars of the holding of beneficial owners received from the depository as of the cut-off date, the issuer or its registrar and transfer agent would distribute dividend, interest and other monetary benefits directly to the beneficial owners.

PLEDGE/HYPOTHECATION

Securities held in a depository account can be pledged or hypothecated against a loan, credit, guarantee etc, availed by the beneficial owner of such securities. For this, it is imperative that both the parties to the agreement, have a beneficiary account with a depository. It is however not necessary that both of them have their depository account with the same participant or same depository. If a beneficial owner intends to create a pledge on a security, owned by him Regulation 58 of SEBI (Depositories and Participants) Regulations, 1998 have to be borne in mind. We here analyse the respective byelaws and Business Rules of NSDL in this context:-

If a Client intends to create a pledge on a security owned by him, he shall make
an application in this regard in the form specified in the Business Rules to the Depository through the Participant, who has his account in respect of such securities.

The pledgor and the pledgee must have an account in the Depository to create a pledge. However, the pledgor and the pledgee may hold an account with two different Participants.

The Participant after satisfaction that the securities are available for pledge shall make a note in its records, of the notice of pledge, and forward the application to the Depository.

The Depository, after receiving confirmation from the Participant of the pledgee through an application made by the pledgee to the Participant in the form specified in Business Rules in this regard, shall within fifteen days of the receipt of the application create and record the pledge and send an intimation of the same to the Participants of pledgor and pledgee.

On receipt of the intimation above, the Participants of both the pledgor and the pledgee shall inform the pledgor and the pledgee respectively of the entry of creation of the pledge.

If the Depository does not create the pledge, it shall within fifteen days of the receipt of application send alongwith the reasons, an intimation to the Participants of the pledgor and the pledgee.

The pledgor or pledgee may request cancellation of the entry of pledge made by making an application in the form specified in this regard in the Business Rules to the Depository through its Participant.

The Participant shall make a note in its records, of the cancellation of the entry of pledge and forward the request to the Depository.

The Depository, after receiving prior confirmation from the Participant of the pledgee through an application made by the pledgee to the Participant in the form specified in Business Rules in this regard, shall cancel the entry of pledge made under Bye Law 9.9.4 and send an intimation of the same to the Participants of pledgor and pledgee.

The pledgee may invoke the pledge made under Bye Law 9.9.4, subject to the provisions of the pledge document, by making an application in the form specified in this regard in the Business Rules, to the Depository through its Participant.

The Participant shall make a note in its records, of the request of invocation of the entry of pledge and forward the request to the Depository.

The Depository, on receipt of a relevant request, shall invoke the pledge and amend its record accordingly to register the pledgee as a beneficial owner of the securities and shall thereafter, send intimation of the same to the Participants of the pledgor and the pledgee.

On receipt of the intimation above, the Participants of both the pledgor and the pledgee shall inform the pledgor and the pledgee respectively of the invocation of pledge.
If the Client intends to create a hypothecation on the securities owned by him, he may do so in accordance with the provisions aforesaid which shall apply mutatis mutandis apply in such cases of hypothecation, except that the Depository shall invoke the entry of hypothecation made after receiving confirmation from the Participant of the hypothecator through an application made by the hypothecator to the Participant in the form specified in this regard in the Business Rules.

No transfer of security in respect of which a notice or entry of pledge or hypothecation is in force shall be effected by a Participant without the prior concurrence of the pledgee or the hypothecatee as the case may be.

IMPORTANT COMPLIANCES TO BE ENSURED BY DEPOSITORY PARTICIPANTS

As a whole it may be mentioned that the following compliances must be ensured by Depository Participants for proper functioning as also to safeguard their own interest as well as interests the of investors.

1. Account Opening

At the time of opening of a new demat account the Depository Participant should ensure that the application form has been filled in all respects and client has been introduced by a known person. Moreover, proof of identity is required to be submitted. The data of new client should be entered into NSDL/CDSL-DPM system and the client should be duly informed about his Client-Id.

It shall be ensured that before opening a DP account, agreement with prospective Beneficial Owner has been entered.

It may be noted that obtaining photocopy of PAN card and its verification has been made mandatory.

2. Reporting to Clients

A Depository participant should ensure that the following information is provided to the client:

(a) Statement of holdings to the client at regular intervals.
(b) Transaction Statement as and when a purchase or sales transaction is carried out.
(c) Allotment details in case of primary market issues.
(d) Confirmation of change in address/bank particulars/nomination etc.
(e) Any bonus shares credited into client’s account.
(f) Confirmation of dematerialisation/rematerialisation requests.
(g) Suppression, freezing or defreezing of accounts.

3. Dematerialisation of shares

In respect of dematerialisation, the following points of action must be ensured by Depository participant:
(a) Dematerialisation Request form (DRF) is accompanied by share certificates. Folio No., Certificate Nos., Distinctive Nos., written on DRF tally with those written on Share Certificates.

(b) Pattern of holding written on Share Certificates conforms with the order of names in which account has been opened.

(c) DRF is completely filled and duly signed. The signatures of client on DRF should be verified from specimen signature as per record with the company/STA.

(d) DP should ensure that the Share Certificates are stamped “Surrendered for Dematerialisation” and two holes are punched on the name of company on Share Certificate.

(e) DP should ensure that separate DRFs are filled for locked-in and free securities having same ISIN.

(f) DP should ensure that separate DRFs are filled by client for securities having distinct ISIN, namely of different companies.

(g) The demat request should be entered in DPM system and the Demat Request Numbers (DRN) generated should be filled at the space provided on DRF.

(h) DRF and Shares Certificates should be forwarded to the Company within 7 days of receipt after filling the authorisation portion of the form.

(i) In case any demat request is returned by the company under objection, DP should inform the client suitably and facilitate rectification/correction of objection so that request can be submitted again.

4. Rematerialisation of Shares

With regard to rematerialisation:

(a) DP should ensure that Rematerialisation Request Form (RRF) submitted by the client is complete in all respects and duly signed.

(b) DP should ensure that the client’s demat account had the sufficient credit balance of shares of the company for which rematerialisation request has been submitted. If it is found that client’s account does not have enough balance, demat request should be rejected and client be intimated accordingly.

(c) The request should be entered in DPM system and Remat Request Number (RRN) generated should be filled on RRF.

(d) The request should be forwarded to the Company/RandT agent after filling the authorisation portion of RRF.

5. Market trades

(i) At the time of sale of shares the selling client submits to the DP a request (Delivery instruction) for transferring balances from his demat account to the pool account of the clearing member through whom he has sold the shares. In the delivery instruction the client should specify the market type, the settlement number of the trading period for the trade for which transfer is executed, the number of shares, execution date and also the CM-BP-Id
(Clearing Member-Business Partner-Identification) of the clearing member in the depository system.

(ii) On receipt of delivery instruction the DP should verify the signature of client from the specimen signature available in records.

(iii) DP should enter the request in DPM and the instruction number should be entered on the delivery instruction form.

SEBI vide circular SMDRP/POLICY/CIR-5/2001, dt 1-2-2001, has stipulated that with effect from 12-2-2001, clearing member is required to transfer the securities from their respective CM Pool Account to the respective beneficiary account of their clients within 6 calendar days after the pay-out day instead of the existing time limit of 15 days. With effect from 2-4-2001, the time limit of 6 calendar days after the pay out day for transferring the balances to the beneficiary accounts of the clients shall be reduced to 4 calendar days or 2 working days whichever is earlier.

6. Pledge and Hypothecation

The shares held in dematerialised form can be pledged by clients for the purpose of obtaining loans from banks. For the purpose of creating pledge, the DP should ensure that:

(a) an application is submitted by the client.

(b) Notice of Pledge should be noted in the records only after ensuring that sufficient security balance(s) is/are available for pledge.

(c) DP should confirm creation of pledge to the Depository within 15 days of the receipt of the application.

(d) DP should inform the pledger as well as pledgee about the creation of pledge.

7. Closure of Account

On receipt of an application in prescribed form from a client for closure of account, the DP should ensure that if any security balances exist in the account then the account is closed only after:

(a) all the shares lying in the account have been rematerialised or;

(b) security balances have been transferred to another demat account.

8. Reconciliation of Records

A Depository participant is not only required to effect internal reconciliation of its accounts on a daily basis but also at the end of each day it must provide to the Depository the details of changes made in the accounts of its clients from last end of day processing.

9. Records to be maintained by a Depository participant

DP should maintain the following records for period of five years:

(a) Form submitted by the client for:
    Opening of accounts.
Closing of accounts.
Freezing of accounts.
Defreezing of accounts
(b) Delivery Instructions given by clients.
(c) Records of all actions taken on the exception reports generated by the
system.
(d) A Register showing details of grievances received from the clients and their
present status.
(e) Instructions received from the clearing member to transfer balances from the
Pool Account to the Delivery Account of the Clearing Member in order to
enable him to deliver these securities to the clearing corporation for
settlement of trades.
(f) Instructions given by clearing member authorising the transfer of securities
from the pool account to the account of its clients.
(g) Dematerialisation Request Forms (DRFs) and Rematerialisation Request
Forms (RRFs) filled by clients.
(h) Forms received in the case of pledge and transmission of securities.
(i) Details of certificates sent for dematerialisation.
(j) Proof of despatch of DRFs and Share Certificates by courier.
(k) Details of certificates, sent for dematerialisation, received back along with
objection memo from various companies.

10. Action to be taken for Rematerialisation of Shares

The shares held in electronic form can be reconverted into physical form and this
process is called rematerialisation. If a shareholder wishes to get his shares
rematerialised, he can approach his DP and submit a Rematerialisation Request
Form (RRF). The company on receipt of RRF and electronic download from
Depository through electronic Registrar rematerialises the shares by issuing a fresh
Share Certificate. It should be noted here that although a new Share Certificate
Number will be generated but the distinctive numbers to be printed on the Share
Certificate will be those which have already been dematerialised. Those distinctive
numbers should be issued which have been dematerialised first. This system will
enable the company to always compare the Demat Register with Remat Register
because entries of Distinctive Nos. appearing first in Demat register will appear in the
same order in Remat Register. As a result of Rematerialisation the shares get
transferred from Depository’s folio in Company’s Register of Members to a new folio
allotted to the shareholder. The Share Certificates should be printed and depatched
to the Depository Participant only after a confirmation/certificate is received from the
electronic Registrar that remat request has been uploaded to Depository.

Records to be kept by a company after its shares and other securities are in the
Demat Mode

Where an existing company has entered into an agreement with a Depository for
dematerialising its shares and gives an option to its members to continue to hold their
certificates or to hold the shares with a Depository, it is a gradual process before all the members opt for the demat mode. However, it may be safely presumed that there may be substantial number of members who may like to continue to hold the Share Certificates. In that case the company shall keep a Register of Members in terms of Section 150 and Index as per Section 151 of the Companies Act, 1956. It will also maintain a Transfer Register for recording particulars of transferors and transferees. The company shall comply with the provisions of Companies (Issue of Share Certificates) Rules, 1960 in respect of the share certificates held by its members.

In respect of a company of the above nature, the company will also get the list of beneficial owners from the Depository from time-to-time. For the purpose of dividend payment, the company will specifically get a list of beneficial owners from the Depository as on close of the day prior to the date from which the Register of Members will closed as per Section 154. In respect of record date, the beneficial owners will be determined as on the close of business on the said date.

**ISIN Number and Listing Approval by Stock Exchange**

It was observed by Stock Exchanges that there has been delay on the part of companies to list further issues of capital either through preferential route or otherwise. However as there is a single ISIN number for all the shares issued by companies except for partly paid-up shares, there is a possibility of such freshly issued shares being delivered in the market without being listed. To deal with this issue, it was decided by all Stock Exchanges at their meeting held on 17th January, 2001, that the Stock Exchanges would electronically upload the “in-principle” listing approval to the Depositories. To start with, this would be done by the major exchanges. This will enable the depositaries to check before dematerialisation whether a company has applied for listing on the Stock Exchanges. Further, the Regional Stock Exchanges would also confirm to the depositaries that the shares of the company have been listed on all the exchanges where the company has applied for listing. The depositaries will only thereafter dematerialise the shares.

**AGREEMENT TO WHICH THE DEPOSITORY PARTICIPANT IS A PARTY**

A DP is required to enter into two important agreements in course of demat trading.

1. Agreement with the Depository; and
2. Agreement with the Investor.

1. **Standard Agreement with the Depository (NSDL)/(CDSL)**

   Important clauses needing compliance on part of the DP are :-
   
   
   (b) Payment of requisite fees and charges as prescribed.
   
   (c) Compliance with valid instructions of the investor and ensuring that holdings of the DP do not comingle with those of its clients.
   
   (d) DP to reconcile its own records with the Depository on a daily basis.
(e) DP to maintain such Hardware and Software Systems as are stipulated by the Depository.

(f) DP to maintain Insurance mechanism and coverage as stipulated by the Depository.

(g) DP to contribute to the Investor Protector fund, the Participant Fund and any other fund established to protect the interests of the clients as may be prescribed by the Depository.

(h) DP to comply with accounting, audit, financial requirements, submission of returns, internal controls, audit control measures as stipulated by the Depository.

(i) DP to notify the Depository within 7 days of any change in the details set out in the application form submitted to the Depository at the time of admission or furnished from time to time.

(j) DP to resolve investor grievances and submit a report to the SEBI and the Depository within the time stipulated by the SEBI Regulations.

2. Standard agreement with the Investor

Important clauses needing compliance by DP are as under:

(a) The DP shall strictly adhere to the instructions of the client with regard to transfer to and from the Accounts of the Client.

(b) The DP shall provide a statement of Accounts to the client at fortnightly intervals unless otherwise agreed.

(c) The DP shall resolve all legitimate grievances of the client within a period of 30 days.

INTERNAL AUDIT OF DPs

The two Depository service provides in India, viz., National Securities Depository Ltd. (NSDL) and Central Depository Services (India) Limited (CDSL) have allowed Company Secretaries in whole-time Practice to undertake internal audit of the operations of Depository Participants (DPs).

NSDL has vide its circular No. NSDL/SG/II/010/99 dated 26th March 1999 notified amendment of its Bye Laws 10.3.1 of Chapter 10 as follows:

10.3.1 “Every Participant shall ensure that an internal audit in respect of the operations of the Depository is conducted at intervals of not more than three months by a qualified Chartered Accountant or a Company Secretary holding a certificate of Practice and a copy of the internal audit report shall be furnished to the Depository.”

CDSL has vide its letter dated September 28, 1999 notified amendment of its Bye Laws 16.3.1 as follows:

16.3.1 “Every Participant shall ensure that an internal audit shall be conducted in respect of the participant’s operations relating to CDS by a qualified Chartered Accountant in accordance with the provisions of the Chartered Accountants Act, 1949 or by a Company Secretary in practice in
accordance with the provisions of the Company Secretaries Act, 1980, at such intervals as may be specified by CDS from time to time. A copy of Internal Audit report shall be furnished to CDS.”

Also, Regulation 55A as inserted by SEBI (Depositories and Participants) (Second Amendment) Regulations, 2003 provides that every issuer shall submit an audit report on quarterly basis to the concerned stock exchanges audited by a qualified Chartered Accountant or practising company secretary, for the purposes of reconciliation of total issued capital, listed capital and capital held by depositaries in dematerialized form, the details of changes in share capital during the quarter and the in-principle approval obtained by the issuer from all the stock exchanges where it is listed in respect of such further issued capital. Further, Regulation 58B stipulates that a depository and a participant shall appoint a Compliance Officer who shall be responsible for monitoring the compliance of the Act, rules and regulations, notifications, guidelines, instructions etc. issued by the SEBI or the Central Government and for redressal of investors’ grievances.

Internal Audit of DPs at quarterly intervals is bound to be a herculean and a highly onerous task. Familiarisation with the technical facets of the demat trading plus a thorough exposure to the practical realities involved in this electronic means, is most called for. The Depositories Act, 1996 empowers the depositaries to make bye-laws relating to ‘internal control standards including procedures for auditing, reviewing and monitoring’. In pursuance of these powers, NSDL has stipulated that every participant shall ensure that an internal audit in respect of the operations of the depository is conducted at intervals of not more than three months by a Chartered Accountant or a Company Secretary, holding a certificate of practice; a copy of the internal audit report shall be furnished to the depository. It is suggested that the audit report may include the following:

(i) instances of non-adherence to the operational procedures prescribed, relating to functions of participant;
(ii) observations about discrepancies or weaknesses in the internal control mechanism;
(iii) comments on the record maintenance;
(iv) comments on the user authorisation and data security systems;
(v) instances of non-compliance with the relevant legislations governing the depository operations;
(vi) general observations and recommendations, if any.

NSDL Byelaws stipulate that the scope of such internal audit of DPs shall cover the existence, scope and efficiency of the Internal control system, compliance with the provisions of the SEBI Act, the SEBI (Depositories and Participants) Regulations 1996, Byelaws, Business Rules, Agreements and Systems security of the DP. The Internal Auditor would need to take up and examine compliance by the DP with all the above referred provisions, Byelaws, Business Rules and terms of the Agreements executed by the DP.

SCOPE AND OBJECTIVES OF INTERNAL AUDIT OF DEPOSITORY PARTICIPANTS

NSDL vide its Circular no NSDL/PI/2002/1271 dated July 30, 2002, has specified
the following objectives and scope of internal audit.

OBJECTIVES OF INTERNAL AUDIT

The following are the broad objectives of internal audit function of a Participant:

(a) To assure the management that the operations of the Participant are in compliance with the requirements of The Depositories Act, 1996, SEBI (Depositories & Participants) Regulations, 1996, NSDL Bye Laws and Business Rules and its agreement with the client and NSDL.

(b) To assure management that the DPM system is managed and maintained in a manner that there is no threat to business continuity, integrity of data processing system is maintained at all times and methods are put in place to ensure that records are not lost, destroyed or tampered with or in the event of loss or destruction of data, sufficient backup of records is available at all times.

(c) To assure management that the capacity of computer system, staff strength and internal procedures are commensurate with the business.

(d) To assure management and NSDL that the business operations of the Participant are conducted in a manner that all the foreseeable risks are addressed to with appropriate internal control mechanism.

(e) To assure management that the operations are conducted in a manner that there is no loss of revenue and receivables are received promptly.

AUDIT PROGRAMME

Internal Audit Programme should cover all facets of operations. An illustrative list of audit points is given below. Internal auditors may expand the scope of audit/add more audit points to achieve the internal audit objectives listed above. In addition, internal auditor may cover areas specific to a Participant like billing, outstanding payments, attempted frauds etc.

I. Audit of Organisational Structure

1. Whether the Participant has adequate infrastructure, including staff, commensurate with the level of activity?

2. Whether the organisational structure is such that the accountability, proper role definitions and segregation of duties are in place?

3. Whether organisational structure and level of supervision are adequate for the number of branches/franchisees and the number of client accounts handled?

4. Whether there is effective system/procedure in place to keep the management informed about exceptional events like problem in hardware or any component of hardware/software, backup, UPS, telephone line, reduction in space to business ratio, staff to business ratio, reducing hard disk space, decreasing speed of machine, etc.

5. Whether there is the effective system/procedure to report exceptional transaction related issues, like failure in delivery instruction, failure of transactions leading to auction of clients, delay in confirmation to clients, loss of certificates sent for demat, complaints from clients that they have not
received credit for the securities etc.? Describe the same.

6. Whether there is a system/procedure for reporting attempted frauds, misappropriation of securities, etc., by clients or by any employee of the Participant/franchisee? Describe the same.

II. Audit of DPM Operations

1. Whether backup is taken on a daily basis as per the procedure prescribed by NSDL (which includes copying the back up files from hard disk to back up tapes) and whether a second copy of the backup tapes is stored at a remote site away from the operational site?

2. Whether Emergency Repair Disk is created fortnightly or immediately after any Hardware/Software configuration changes made in the server, whichever is earlier? (Circular No. NSDL/PI/2002/1262 dated July 29, 2002)

3. Whether back up of RAID Controller Configuration taken on monthly basis or immediately after disk / Raid controller repairs/upgrade is made, whichever is earlier? (Circular No. NSDL/PI/2002/1262 dated July 29, 2002)

4. Whether back up of speed-e downloads (including digital signature) taken and a copy of the same is sent to remote site?

5. Whether the procedure and frequency of download and upload of response file from the speed-e server as per NSDL requirements (at least three times in a day)?

6. Whether the DPM system is working satisfactorily without any downtime and whether systems support for its hardware is available at all times from its vendors?

7. Whether size of the equipment/memory/disk-space, backup tapes etc., are maintained in relation to level of business operations?

8. Whether all the equipments are under appropriate AMC/warranty?

9. Whether the variable access scheme as suggested by NSDL (association of DPM users to proper groups, rights given to user groups as per the requirements, maker checker concept) has been put into operation?

10. Whether alternative method of communication with NSDL, namely dial-up, is working or not?

11. Whether the DPM system is physically and logically well protected from unauthorised access?

12. Whether anti-virus software is loaded as well as upgraded from time to time (immediately as and when available) on the DPM system?

13. Whether the circulars and other information sent by NSDL on the MS Exchange is read regularly?

14. Whether any external software other than the DPM software, SQL, Windows NT, Internet Explorer, MS Exchange or any other software specifically permitted by NSDL is found loaded on the DPM system?

15. Whether the DPM system is connected to LAN/WAN of the Participant with the permission of relevant authorities?
III. Audit of Account opening procedures

1. Whether proof of identity and residence is collected as per NSDL requirements? (Circular No. NSDL/PI/2000/1394 dated April 09, 2000)

2. Whether necessary documents are collected from clients such as corporates, NRIs, OCBs, FIIs, etc.?

3. Whether necessary documents are collected from Speed-e users at the time of opening speed-e account, resetting password, adding pre-notified accounts etc.

4. Whether the procedure for dispatch of the smart card and the PIN (in case of Speed-e users) is diligently followed by the DP, i.e. sending the smart card and the PIN separately?

5. Whether DP has maintained the records in its internal database with respect to details of Speed-e application forms as per NSDL requirements?

6. Whether an agreement is executed with every client?

7. Whether each client is given copy of the agreement, schedule of charges and ‘Client Master Report’?

8. Whether there is a system in place to ensure that the client accounts are not opened in the name of the partnership firm, proprietorship firm or in the name of HUF?

9. Whether clients signatures have been appropriately stored in physical form and scanned into the system?

10. Whether data entry in the system is strictly and completely in accordance with the information furnished by the client in the account opening form and as per NSDL requirements? (Circular No. NSDL/PI/99/119 dated July 22, 1997 and circular no. NSDL/PI/2000/2295 dated April 18, 2000)

11. Whether there is adequate mechanism to ensure that all the account opening forms accepted are in fact entered in the DPM system and the client is given the client Id only after account comes in ‘Active’ status? (Circular No. NSDL/PI/98/583 dated November 18, 1998)

12. Whether there is a mechanism in place to ensure that the changes in the demographic details are updated in the DPM system (say for change of address, etc.) based on proper authorisation and only after collecting new proof of address from the client. (Circular No. NSDL/PI/2001/1442 dated September 21, 2001)

13. Whether the procedure followed for opening the accounts and servicing illiterate person followed as per NSDL requirements? (Circular No. NSDL/PI/2002/0709 dated May 03, 2002)

14. Whether any supplementary agreement/letter of confirmation etc. is executed in addition to standard DP-Client agreement? If yes, whether any of the clauses appears to be contradictory to standard DP-Client agreement?

15. Whether adequate documents maintained for closure/freezing/unfreezing of client account? This includes the procedure followed by the Participant in respect of accounts, which did not have any balance at the time of closing
IV. Audit of demat requests

1. Whether there is a system/procedure in place to prevent acceptance of securities, which are not admitted to NSDL system?
2. Whether demat requests received are sent to the registrars within seven days from the date of receipt of the request from the clients?
3. Whether there is a system in place, which ensures that certificates are sent by the Participant to the correct address of the Issuer/Registrar & Transfer Agent?
4. Whether there is a system/procedure in place to inform the client in case of rejection of demat request?
5. Whether there is system/procedure in place for mutilating/defacing certificates in the prescribed manner received for dematerialisation?
6. Whether there is a provision for safekeeping the securities received until they are despatched to Issuer/Registrar & Transfer Agent?
7. Whether there is a system in place to analyse the reasons for demat rejections, demat delays and taking corrective actions, especially, when the rejections or delays are attributable to the Participant?

V. Audit of delivery instructions

1. Whether and how all the clients have been informed about the schedule of acceptance deadlines for delivery instructions?
2. Whether there is a system in place to date and time stamp all the delivery instructions received from the clients on both the Participant copy and the client’s copy? (Circular No. NSDL/PI/98/519 dated October 13, 1998)
3. Whether there is a system in place to suitably stamp the delivery instructions received beyond the aforementioned deadlines as received at clients’ risk and would be executed on a best effort basis? (Circular No. NSDL/PI/2002/0583 dated April 08, 2002)
4. Whether the delivery instruction slips issued to clients (including inter depository transfer instruction slips) have pre-stamped client Id and pre-printed serial number and there is control over issue of instruction slips to the clients?
5. Whether delivery instruction booklets are issued to the clients based on the requisition slips only?
7. Whether there is control over blank instruction booklets?
8. Whether there is control over instruction slip number at the time of acceptance from the clients? If yes, whether the slip number validation is done manually or in back office software? (Circular No. NSDL/PI/2000/834 dated June 02, 2000)
9. Whether adequate information is made available to clients on DP-ids, ISINs, Corporate Action details etc.?

10. Whether the client instructions are being executed in DPM system as per the execution date given by the clients?

11. Whether there is a system in place to monitor successful execution of instructions keyed in the DPM system?

12. Whether the instructions are executed as per the delivery instruction form given by the clients? The auditor should also verify the signature of the client and fully satisfy that instruction is indeed given by the client himself.

13. Whether adequate measures have been taken to protect the Participant in case fax instructions are accepted? Whether it is ensured that original instructions are collected within two days and is there a system in place to prevent the double execution of the same instruction? (Circular No. NSDL/PI/2002/0740 dated May 09, 2002)

14. Whether there is a system in place to inform the client in case of failed instructions? If yes, describe the same.

15. Whether there is a system/procedure in place to rectify erroneous transfers done by the Participant or any other Participant. If yes, describe the same.

16. If the Participant is accepting delivery instructions accompanied by computer print-outs from the Clearing Members/Clients, whether the conditions prescribed for such acceptance are being met? (Circular No. NSDL/PI/99/572 dated July 21, 1999 and circular no. NSDL/PI/2000/500 dated April 18, 2000)

VI. Audit of other transactions/services

1. Whether there is a system in place to ensure that transaction statements are provided to the clients’ at least as per the prescribed schedule and in the format prescribed in the Business Rules of NSDL? (Circular No. NSDL/PI/98/823 dated October 20, 1999, NSDL/PI/2000/103 dated January 31, 2000 and NSDL/PI/2002/0398 dated March 07, 2002)

2. Whether there are adequate procedures/systems in place for diligent execution of pledge instructions?

3. Whether the transmissions effected, if any, have been done in accordance with the procedure stipulated by NSDL?

4. Whether remat/repurchase transactions effected, if any, have been done in accordance with the procedure stipulated by NSDL?

5. Whether stock-lending transactions effected, if any, have been done in accordance with the procedure stipulated by NSDL?

6. Whether there is a system in place to record and redress all the grievances of clients arising at the controlling office or at the branch/franchisee within the stipulated time of 30 days?


VII. Audit of branches/franchisees
1. Whether DP is operating through branch/franchisee?
2. Whether branches/franchisees have displayed the type of depository services being offered? (Circular No. NSDL/PI/2000/1531 dated August 24, 2000)
3. Whether the branches/franchisees are appointed after due diligence, appropriate agreements are entered/renewed and whether the Participant reviews activities of its branches/franchisees activities?
4. Whether the scope of activity of the branch/franchisee is clearly documented and adhered to?
5. Whether each branch/franchisee employ trained (as well as NCFM qualified) staff appropriate to the type of function allocated?
6. Whether permission for appointment of franchisee has been obtained from NSDL?
7. Whether the services of any of the franchisees have been terminated by the Participant? If yes, whether the same has been done as per NSDL requirements? (Circular No. NSDL/PI/2002/0346 dated February 26, 2002)
8. Whether branches/franchisees have adequate infrastructure for the current as well as expected level of operation?
9. Whether branches/franchisees are provided with the relevant and critical information/circulars like securities admitted to depository, bye laws, business rules, format/stationery, methods of feedback to clients, viz., demat rejection, failure of delivery out, credits received, etc.?
10. Whether there is a control, co-ordination and the supervisory set up for reporting events that have occurred at branches/franchisees that require management intervention? Describe the same.
11. Whether due diligence is carried out at branches/franchisees while receiving account application forms. This includes whether the account opening forms are properly and completely filled in and branch/franchisee is satisfied about the identity and the credentials of the client?
12. Whether demat requests are sent by the branch/franchisee directly to Issuer and/or R & T agent? If yes, how is it ensured that the same are sent within seven days from the receipt of the same from clients. If no, are the branches/franchisees sending the DRFs to the branches within such time which will enable controlling office to dispatch DRFs to Issuer & R & T agent within seven days from the date of receipt by the branches/franchisees?
13. Whether branches/franchisees have means to verify signatures of the clients before actually sending instruction slips to the controlling office. If no, are the branches/franchisees acting merely as collection centres?
14. Whether any kind of reconciliation between the branches/franchisees and controlling office takes place for the purpose for keeping record of account opening forms, demat requests, instruction slips (including receipt of instruction slips by main office well within NSDL deadline time) and blank instruction booklets issued by and/or received from the branches/franchisees?
VIII. Back office software

1. Whether DP uses the back office software for the purpose of depository related activities?

2. What activities are carried out in the back office with respect to depository related activities? (e.g. data entry with respect to Account opening, demat, remat/repurchase, settlement, pledge, Stock Lending and Borrowing, Statement of Transactions etc.)

3. Whether there is a stationery control (slip number validation) in the back office with respect to the following? (Circular No. NSDL/PI/2000/834 dated June 2, 2000)

4. Record of issuance of delivery instruction slips to the clients including issuance by branches, if any;

5. Receipt and processing of instruction slips received from clients;

6. Provision for blocking of instruction slip numbers, which are already used or reported lost/misplaced/stolen.

7. Whether Statement of Transactions are (or any other reports like client master report etc.) sent from the back office? If yes, whether the details of the same matches with statement or report generated from DPM?

8. Whether back office (including web site) is updated regularly for the transactions done on the DPM?

9. Whether the back up of data residing in back office (or any data maintained in electronic form) with respect to depository operations is taken daily?

IX. Scope of audit for records and documents maintained

1. Whether the following records are being kept in a manner that they can be retrieved at any time:

2. Application forms and agreements with all clients.

3. Register of documents/certificates received for dematerialisation.

4. Record of documents sent for dematerialisation.

5. Instruction slips signed by clients for account transfer, delivery out, pledge, securities lending and borrowing, inter-settlement transfer, inter depository transfer instructions, account closure etc.

6. Register for transaction statements provided to clients giving details such as date of despatch, no. of clients to whom the statements were despatched etc.

7. Investor Grievance Register


9. Whether records are kept separately for each depository?

10. Whether all formats used by the Participant are in conformity with NSDL prescribed format?

11. What is the sampling plan (the manner in which samples are selected for documentation), sample size, approximate man-hours spent and level of
persons engaged for this work. In case any point / comment is of confidential nature, auditor may communicate it separately to NSDL.

X. Information provided to NSDL

Whether the following information/reports/dues are being sent to NSDL in the prescribed format and within the time stipulated by NSDL:

1. Annual Report
2. Networth Certificate and Computation Sheet
3. Internal Audit Report
4. SEBI Annual Fees
5. Dues to NSDL
6. Replies to specific information/compliance required by NSDL

AUDIT REPORT

The audit report should state the scope, objectives, period of coverage and nature and extent of audit work performed. It must mandatorily contain observations on all the audit points given above highlighting the exceptions. The audit report should contain the following:

1. Findings, conclusions, recommendations, reservations and qualifications.
2. Areas where the internal controls are weak or do not exist.
3. Areas where internal controls exist, but exceptions are observed.
4. If any major/significant deviation is observed, the same should be reported separately in the covering page of the audit report.
5. If observation is in the nature of a deviation or a recommendation by the auditor, management response should be sought and recorded in the report. (Circular No. NSDL/PI/2001-0467 dated April 04, 2001).
6. Comment by auditor on whether management has taken necessary action as stated in the management’s response in last audit report.
7. Improvements brought about in the operations between the last audit and the current audit. (Circular No. NSDL/PI/2001-0847 dated June 15, 2001)
8. Comments by the auditor on the remedial action taken by the Participant on the observations made by NSDL. (Circular No. NSDL/PI/2001-0847 dated June 15, 2001)
9. A statement by the auditor that this circular was read, understood and the internal audit report is based on the guidelines given in this circular.
10. A statement by the auditor that the auditor is neither related to officials of DP and/or does not have any interest in the management of the DP nor has any partner/proprietor in the firm who is also a DP official.
11. Auditor’s membership number should be mentioned at the end of the report.
12. If auditor wishes to do ‘Exceptional reporting’ a statement ‘All applicable areas given in the circular above have been verified & found satisfactory.'
This report gives deviations only’ should be made by the auditor.

It may be noted that for the purpose of compliance with Bye Law 10.3 of NSDL, the internal audit must be in accordance with the aforesaid guidelines.

**Checklist for Internal Audit of Operations of Depository Participants**

The Checklist points stated below are common to DPs of both NSDL and CDS unless specifically distinguished.

**1. Account Opening**

To ensure the following:

(i) That all new account holders had been introduced by known person(s) as far as possible in the prescribed forms.

(ii) That the participant has obtained any one of the following from the Beneficial Owner (BO):

(a) Voter-Id
(b) Xerox of passport
(c) Xerox of driving licence (with photograph)
(d) Xerox of Ration Cards.
(e) Any other identification from Government/Banking Institution
(f) Photocopy of PAN Card (mandatory)

(iii) That the photographs of all the account holders had been duly affixed and not stapled.

(iv) That all the account holders had signed across the photographs.

(v) That each account had been opened separately for sole and joint holding and also for each sub-status of the Investor/Beneficial Owner (BO).

(vi) That the agreement between Depository Participant (DP) and the BO seeking to open the account had been signed by both the parties and bears the signatures of witnesses. Also every page had been initialed.

(vii) That the following details had been duly filled, in the application form:

(a) Name of the BO
(b) Address, Telephone Nos. Fax No.
(c) Status code, sub-status code.
(d) Bank Account particulars such as name of the Bank and its Branch, Current Account/Saving Account and details to ensure that 9 digit code of the Bank and Branch appearing on MICR Cheque issued by Bank, has been furnished.

(e) Details of IT Circle/Ward/Dist. No. and PAN/GIR Number, have been furnished.

(f) Signatures of BO/authorised signatories.
(g) In specimen signature-card, signature of BO/authorised signatories and their passport size photograph.

In addition to the above stated particulars, the following details were also given:

In case of Individual:
- Father/Husband's name.
- In case of minor, Date of Birth and details of guardian furnishing the name, relationship (if any) along with the complete address.
- Occupation of BO.
- Nominee’s Name and Address.

In case of NRI:
- Date of Approval of RBI/FIPB.
- Type of Foreign address.
- RBI Ref. No. and Account, whether with or without repatriation.
- Nominee’s Name and Address.

In case of Corporates check that the following had been furnished:
- Certified true copy of Board resolution appointing authorised signatories and their names, designation and specimen signatures or the Power of Attorney given to authorised signatories;
- In case signature have been attested by Magistrate/Notary public/Special Executive Magistrate, their name address, telephone no. etc., have been furnished;
- A copy of the Memorandum and Articles of Association;
- One passport size photograph of each of the authorised signatories with their signatures across the face of the photograph.

In Case of Clearing Members, FIs and OCBs check if the following information/documents had been furnished:
- Power of Attorney (if applicable)
- Certified true copy of Board resolution appointing authorised signatories and their names, designation and specimen signatures.
- In case signatures had been attested by Magistrate/Notary Public/Special Executive Magistrate, his name, address, telephone no. etc.
- A copy of the Memorandum and Articles of Association (if applicable)
- One passport size photograph of each of the authorised signatories with their signatures across the face of the photograph.
- In case of FIs and OCBs, a copy of the approval of RBI if applicable.

(viii) That the account opening form had been duly filed along with the agreement in duplicate and charges as prescribed in ‘Schedule of Charges’ had been furnished to the DP.

(ix) That a standing instruction for automatic credits of securities into the account had been signed by the BO. (However, the standing instruction form is not mandatory).
(x) That the DP had opened the account on completion of necessary requirements, within a reasonable period of time stipulated by the concerned Depository and that while opening the account, the DP had ensured that there were no Data entry mistakes also that full data (including BOs’ signatures) as furnished by the BO had been entered and updated in their (NSDL-DPM/CDS-DP front end) system. A BO Account Number was generated and recorded in the Account Opening Form.

(xi) That details of account entered and generated from the system were sent to the BO.

(xii) Details of PAN Card of BO has been duly verified with the website of IT Deptt.

2. Obligations of Participants towards BOs

To check that whether:

(i) Participant had conducted business with its BOs after entering into an agreement as per Bye-laws of Depository (Annexure B of NSDL Bye-Laws/Annexure C of CDSL Bye-laws) except in case of FIs who had signed custodial agreements and where the account was opened by the custodian acting as a DP;

(ii) Participant had opened separate accounts of each of its BOs for holding security balances on behalf of its BOs;

(iii) Credit or debit to the BO’s account had been given after due authorisation from the BO. The credit/debit instruction form was signed by all the account holders jointly;

(iv) Participant acted on the instructions of the BOs;

(v) Participant was maintaining a separate account for each BO and had ensured that the securities of the BO were not mixed with its own securities.

(vi) Any act done by the DP on behalf of its BO was duly authorised by the concerned BO in writing.

3. Reporting to BO(s)

To ensure that Depository Participant had reported the following information to the BO(s):

(i) Statement of holdings at regular intervals

(ii) Fortnightly transaction statement and if there was no transaction then quarterly statement. (However, the periodicity of statement i.e. fortnightly is not laid down by CDS).

(iii) Allotment details in case of primary market issues.

(iv) Confirmation of change in bank mandate.

(v) Non-monetary benefits like rights, bonus, conversions etc.

(vi) Confirmation(s) of dematerialisation or rematerialisation request(s).

(vii) Suspension, freezing or defreezing of accounts.
4. Dematerialisation of securities

To check that:

(i) BO had submitted to the DP, the securities for dematerialisation along with the Dematerialisation Request Form (DRF).

(ii) That all Demat Requests had been received from BOs, whose accounts had been opened in the same order as mentioned on share certificates.

(iii) No dematerialisation request had been entertained by the participant other than from a registered holder of securities.

(iv) Requests accepted for dematerialisation belong only to those securities declared by the Depository as ‘eligible’ for dematerialisation, as on the date of acceptance of the DRF. Also to ensure that certificates accepted for demat pertain to the distinctive number ranges as intimated by the Issuer and communicated to DPs.

(v) The DRF submitted by the BO had been completely filled and duly signed.

(vi) The DP had issued a system generated Acknowledgement of the Demat Request after putting his seal/rubber stamp and signature of the authorised signatory, to the BO.

(vii) The DP had duly verified the signature of the BO, as on the form, with the specimen available in its records.

(viii) In case of signature mismatch, the DP had not accepted/processed dematerialisation request.

(ix) The details of the certificates submitted for dematerialisation were in consonance with the details filled up in the corresponding DRF.

(x) The certificates submitted for dematerialisation had been marked by the BO with the words “Surrendered for Dematerialisation”.

(xi) The DP had ensured the safety and security of the certificates submitted for dematerialisation till the certificates were forwarded to the Issuer or its Registrar and Transfer Agent.

(xii) The DP had ensured that a separate DRF had been filled in by the BO for securities having distinct International Securities Identification Numbers (ISINs).

(xiii) The DP had ensured that a separate DRF had been filled in by the BO for locked-in and free securities having the same ISIN.

(xiv) The DP had ensured that the BO(s) had submitted a separate DRF for each of his/her/their/it’s accounts maintained with the DP.

(xv) The DP had punched two holes on the company name on the security certificates in the manner laid down in Business Rules before forwarding the same to the issuer or its R and T Agent.

(xvi) The DP has verified that the pattern of holdings in the account of the BO matched with the pattern of holdings as per the security certificates.

(xvii) Details recorded for the Dematerialisation Request Number (DRN) were verified by a person authorised to verify the request as per the Access
Authorisation Scheme recommended by Depository (i.e. the function of capture and verify release is done by two different users). In case of CDS there is no system of verify release as stated above and transactions are to be entered and committed.

(xviii) The DP had forwarded the DRF to the Issuer or its Registrar and Transfer Agent only after ascertaining that the number of certificates annexed with the DRF tallies with the number of certificates mentioned on the DRF, within 7 working days of its receipt.

(xix) In the case of securities which had been submitted for dematerialisation for which any objection memo had been received from the Issuer or its Registrar and Transfer Agent, the DP had facilitated the correction of such objections within reasonable time.

(xx) DP had diligently followed the pending cases of Dematerialisation of securities.

5. Rematerialisation of Securities

To ensure that the following system was followed in rematerialisation of securities:

(i) The BO(s) submitted a request to the DP for rematerialisation of holdings in his/her/their account.

(ii) On receipt of the request form (RRF), the DP had verified that the form was duly filled in and had issued to the BO an acknowledgement slip duly signed and stamped.

(iii) The DP had duly verified the signature of the BO as on the form with the specimen available in its records.

(iv) In case of signature mismatch, DP had not accepted / processed rematerialisation request.

(v) If the form had been in order the DP had entered the request details in its NSDL-DPM/CDS-DP-front end system. While entering the details if it was found that the BO’s account did not have enough balance, the DP had not entertained the request.

(vi) The DP had intimated the BO that the request could not be entertained since the BO did not have sufficient balance.

(vii) The RRN so generated was entered in the space provided for the purpose in the rematerialisation request form.

(viii) Details recorded for the RRN were verified by a person authorised to verify the request as per the Access Authorisation Scheme recommended by Depository (i.e. the function of capture and verify release is done by two different users. In case of CDS there is no system of verify release as stated above and transactions are to be entered and committed).

(ix) The DP forwarded the request to the Issuer/RandT agent electronically.

(x) The DP had filled the authorisation portion of the request form.
(xi) The DP had dispatched the request form to the Issuer/R&T agent within 7 days of accepting such request from the BO.

(xii) The DP had informed the Issuer/R&T about the changes in the BO account, following the acceptance of the request.

6. Maret trades

(A) Authorisation for debit (delivery)

To ensure that:

(i) The selling BO had submitted a request to the DP for transferring balances from its account to the Pool of the CM through whom the BO intended to settle his trade. The BO had specified the market type and the settlement number of the trading period for the trade for which transfer was being executed, the quantity of security, execution date and also the “NSDL-CM-BP-Id/CDS-CM ID” of the clearing member in the depository system.

(ii) On receipt of the request the DP had verified that the form was duly filled in and that the signature as on the form tallied with the specimen signature available in its records. Also that for jointly held accounts all holders had signed the form.

(iii) If the signatures were different, the DP had not processed the request under any circumstances.

(iv) The DP had checked the target DP’s DP-Id on the form.

In case of DP of CDS check whether the following procedure was followed:

(1) Where Clearing House (CH) provides facility to settle trades at the BO level check that:

   (i) DP had been monitoring the on-market confirmation instructions entered by them. In case of a mismatch DP had taken steps to rectify the error.

   (ii) The follow up by the DP was done before pay-in-time.

   (iii) The unmatched sale obligations and the short quantity had been communicated by the DPs to the BO.

(2) In case the Clearing House does not permit a BO level settlement and does a Clearing Member level Settlement only, check that the following procedure was adhered to:

   (i) The BOs transferred the securities to the Clearing Member's clearing account.

   (ii) At the time of pay-out the receiving obligations were credited directly to the Clearing Account.

   (iii) The DPs had ensured that all transfer instructions given by the CMs were executed promptly.

(Note: The treatment of transfer of Securities between the BOs to the CMs is treated as part of on-market transfers by NSDL and as off-market transfers...
(B) **Intra-DP transfer**

To ensure that:

(i) If the target DP’s DP-Id was the same as its own DP-Id, the DP had entered the request in the DPM as an intra-DP transfer.

(ii) The DP had entered the request in the DPM, and the system had generated an instruction number for the request. The DP had verified and released the instruction.

(iii) The execution date entered by the DP was as provided by the BO. For alterations made in case of transactions not being executed on the date as specified by the BO, the same should be executed after obtaining BO’s authorisation. In case the execution date entered happened to be a holiday, the transfer was executed on the next business day following the holiday.

(iv) If sufficient free balance was not available in the BO account on the execution date, the request had been marked as ‘overdue’ by the system. If there were no sufficient balances available in the account till the end of the regular operations for business day, the order was rejected by the DPM. Part delivery, to the extent of free balance available, had not taken place.

(v) In the event of such rejection, the DP had intimated the BO that sufficient free balance was not available in his/their account for executing the transfer.

(C) **Inter-DP transfer**

To ensure that:

(i) While verifying the transfer request form, if the DP had found that the target DP’s DP-Id was different from its own DP-Id, then it had initiated an inter-DP transfer.

(ii) The DP had entered the request in the DPM/front-end system and the DPM/front end system generated an instruction number for the request. The DP had then verified and released the request.

(iii) The DP had complied with the date and time stamping requirement of Depository.

(Note: CDS maintains a Central Data base. Thus there is no distinction between Intra-DP and Inter-DP transfers)

(D) **Authorisation for credit (receipt)**

To ensure the compliance of the following:

(i) A BO executing purchases in the depository segment was required to give a credit authorisation to its DP, in case no standing instruction was given.

(ii) The buying BO submitted request to the DP to transfer securities to its own account.

(iii) On receipt of the request, the DP verified that the form was duly filled in and
in case of signature difference the DP had not processed the request.

(iv) If the Target DP’s DP-Id was the same as its own DP-Id, the DP entered the request as Intra-DP transfer. On the execution date, the corresponding BO’s account was credited. (It may be noted that in case of DP of CDS there is no distinction between Intra-DP and Inter-DP transfers).

(v) If the target DP’s DP-Id on the form was different from its own DP-Id, the DP entered the request in the DPM as inter-DP transfer.

(vi) In the event of rejection, the DP intimated the same to the BO.

(vii) Status of the request was automatically updated in the instruction details stored in the DPM.

(viii) The DP had complied with the date and time stamping requirement of the Depository.

7. Off-Market Trades

To check that:

(i) The transferor/delivering client has submitted a request to DP in prescribed form for transferring balances from its account to another account.

(ii) On receipt of the request, the DP had verified that the form is duly filled-in and signed. If the form was found in order, the DP entered the request in DPM.

(iii) On the execution date mentioned in the instruction form DM initiated transfer if the debit instruction thus released to DM was matched by a complementary credit instruction coming to DM from the counterpart’s participant.

(iv) The transfer was effected by DM and intimated to DPM, and it has debited the transferor clients’ concerned blocked holdings and up-to-date status of the request.

8. Transmission

(A) In case of death of the sole holder for transmission of securities check that-

(i) The legal heir(s) or legal representative(s) of the deceased had made a request, in the prescribed form, to the DP for transmitting the balances lying in the account of the deceased to their account. (A single request would be sufficient for all the securities held in the deceased’s account.)

(ii) The following documents were submitted along with the request for transmission

(i) A copy of the death certificate duly notarised.

(ii) A copy of the succession certificate duly notarised or an order of a court of competent jurisdiction where the deceased had not left a Will; or

(iii) A copy of the Probate or Letter of Administration duly notarised.

Where the market value of the securities held in each of the accounts of the deceased as on the date of application for transmission had not exceeded Rs. 100,000 request for transmission were either accompanied by:
(i) A copy of death certificate duly notarised;
(ii) Letter of Indemnity duly supported by a guarantee of an independent surety acceptable to the participant, made on appropriate non-judicial stamp paper;
(iii) An affidavit made on appropriate non-judicial stamp paper; and
(iv) No objection certificate(s) from all the legal heir(s) who do not object to such transmission.

(OR)

(i) A copy of death certificate duly notarised;
(ii) A copy of succession certificate duly notarised or an order of a court of competent jurisdiction where the deceased had not left a will; or
(iii) A copy of the probate or letter of Administration duly notarised.

After effecting the transmission, the participant had closed the account of the deceased.

(B) Transmission in Case of Death, Lunacy, Bankruptcy, Or Insolvency of One or More of the Joint Holders

In the event of death, lunacy, bankruptcy, or insolvency of one or more of the holders in a joint account, check that:

(i) The surviving holder(s) had requested the DP to transmit the balances lying in the client account to the individual(s) account.
(ii) The request for transmission had been made to the DP in the prescribed form along with a copy of the duly notarised death certificate.
(iii) On receiving such a request, the DP had verified the death certificate and the signature(s) of the surviving client(s).
(iv) The DP had effected transfer of the balances to the new account(s) opened in the name of the surviving client(s) and closed the old account held in the name of joint holders including the deceased holder after being fully satisfied on all aspects.

9. Returns to Depository

To ensure that the DP has submitted the following returns to the depository within the time limits specified:

(i) Net worth certificate computed in manner laid down in the NSDL Business Rules/CDS Bye-Laws Annexure A, duly certified by a Chartered Accountant on audited annual accounts of the DP;
(ii) In case the DP is a clearing member of the clearing corporation, the details regarding any suspension/termination or defaults or any disputes in relation to its dealings with such clearing corporation.
(iii) Number of complaints received from BOs their nature, status and manner of redressal once every month;
(iv) In case of CM-DP, it has informed the Depository when the aggregate market value of securities exceeds the limits specified by SEBI.
10. Collateral security

To ensure that the DP-
(i) Provided on demand, collateral or additional collateral;
(ii) Had not created or permitted the creation of any mortgage, charge or other encumbrance, overall on any of the assets provided as collateral.

11. Indemnifying the Depository

To ensure that the DP indemnified the depository and its officers and employees and held each of them harmless against all costs, fees, expenses, liabilities, actual losses, taxes, levies and damages of any nature whatever suffered or incurred by any of them in respect of following matters:
(i) The participation in the Depository System;
(ii) Failure by the DP to comply with provisions of the Bye-Laws and DP agreement or any other directions of depository;
(iii) Failure of DP to give instructions to the Depository as contemplated in the Bye-Laws;
(iv) The acts of Depository or its officers and employees by placing reliance upon the instructions or communications believed to be given by DP;
(v) Acceptance by the Depository of eligible securities deposited by the DP and giving effect to transactions relating thereto by the Depository in accordance with the Bye-laws and thereunder the withdrawal of eligible securities by the DP;
(vi) The failure by the DPs to deliver eligible securities, or to perform such other duties or obligations contemplated in the Bye-laws, Business Rules, Circulars, directives etc. as may be issued by Depository from time to time;
(vii) As a result of or in connection with the purchase or replacement of eligible securities by the Depository on behalf of the DP.

12. Replacement of Securities (in case of NSDL-DP)

To check that the DP had done the following where a negative balance arose as a result of rectifications by depository of any erroneous credit entries to its accounts:
(i) he had replaced the relevant eligible securities in this connection as may be required by the Depository;
(ii) he had paid forthwith a sum in cash as directed by the Depository as collateral.

(Nota: In case of CDS there cannot be a negative balance in any account in the Depository system.)

13. Assignment of Business

To ensure that the DP had not assigned its business as a DP to any other person except with the prior approval of the Depository.

14. Freezing of Account
To ensure that the DP:

(i) Froze the account of a BO maintained with it only on written instructions received by it from the BO in the form specified under the Business Rules;

(ii) Froze the account of a BO on written instruction received by it from the Depository pursuant to the orders of the Central or State Government, SEBI or any order passed by the court, tribunal, or any statutory authority in this regard.

15. Closure of Account

Check that:

(i) The BO had made an application, in the format specified to that effect. In case the DP has initiated closure (only in the case of CDS), whether approval from CDS has been obtained.

(ii) That if no balances are standing to credit in the account of the BO the account was closed.

(iii) In case any balances existed, then the account was closed in the following manner;

(a) by rematerialisation of all the existing balances in the account; and/or;

(b) by transferring the security balances to the other account of the BO held either with the same DP or with a different DP.

(iv) The DP had ensured that all pending transactions as well as suspended accounts had been adjusted before closing such account. After ensuring that there were no balances in the BO accounts, the DP had executed the request for closure of the BO’s account.

16. Pledge and Hypothecation

(A) Creation of Pledge

To check that

(i) An application was made by the BO for such purpose;

(ii) The Pledger and pledgee both have an account with the same Depository;

(iii) DP had noted in its records the notice of pledge/executed the instructions of the pledge only after it was satisfied that the securities were available for pledge.

(iv) DP had confirmed creation of pledge to the Depository within 15 days of the receipt of the application.

(v) DP had informed the pledger or pledgee of the entry of the creation of pledge.

(B) Cancellation of Pledge

To check that

(i) An application was made by the BO in this regard;
(ii) DP had noted in its records the cancellation of the entry of pledge and forwarded the request to the Depository in case of NSDL;

(iii) DP gave confirmation to the Depository;

(iv) DP informed the pledger/pledgee accordingly of the entry of cancellation of pledge.

In case of hypothecation (only in case of NSDL as CDS does not permit hypothecation) on securities all the above points shall apply mutatis mutandis.

17. Invocation of Pledge/Hypothecation by Pledgee

In case the pledger failed to discharge his obligations under the agreement of pledge/hypothecation, the pledgee has invoked pledge/hypothecation to claim the beneficial ownership of the pledged/hypothecated securities. In such a case check that:

(i) The pledgee had submitted a request in the prescribed form to his participant for invoking the pledge/hypothecation.

(ii) The participant had verified the form for its completeness and validity and if not found in order had returned the same to the pledgee for rectification.

(iii) If the form was found to be in order, the participant had accepted the form for processing and had issued an acknowledgment for the same to the pledgee.

(iv) The participant had also compared the details on the form with the details displayed at DPM against the pledge/hypothecation instruction number.

(v) The participant had entered the invocation request details in DPM against the pledge/hypothecation instruction number as per the instructions given in the form and released the instruction to the depository.

(vi) On receiving intimation of invocation, the pledger's participant had furnished the details of the pledge/hypothecation requests to the pledger.

(vii) The pledgor had instructed its participant, in the prescribed form, to accept/reject the invocation request.

(viii) The pledgor had submitted his acceptance/rejection of the closure request in the prescribed form.

(ix) The participant had verified the form for its completeness and validity and if not found in order return the same to the pledgor for rectification.

(x) If the form was found to be in order, the participant had accepted the form for processing and had issued an acknowledgement for the same to the pledgor.

(xi) The participant had also compared the details on the form with the details displayed at DPM against the pledge/hypothecation instruction number.

(xii) On receiving the instructions from the pledgor, the participant had executed the order for accepting/rejecting the invocation request in DPM as per the instructions given in the form.

(xiii) In case of rejection by the pledgor, the participant had entered the reason for rejection in DPM as specified in the form.

(xiv) The acceptance/rejection of invocation confirmation had been communicated to DPM of the pledgee's participant through DM.
In case of rejection by the pledgor, the securities had continued to remain as pledged.

Balances in the pledgor’s account and the reasons for rejection had been displayed in DPM of the pledgee’s participant.

Upon acceptance of invocation of a pledge, the securities had been transferred from the pledged balance of the pledgor to the credit of pledgee’s beneficial owner account.

The intimation of the same had been given to the pledgor’s participant through DM and the status of the pledge had been changed to “closed, invoked”.

18. Lending and Borrowing of Securities

(A) Deposit of Securities by Lender with Intermediary

To check that:

(i) A beneficial owner of securities who had desired to participate in a securities lending program had submitted a securities lending request form, in the prescribed manner, to his participant.

(ii) The participant had verified the lending request form for its validity and completeness and had executed the instructions as per the specifications made in the form.

(iii) After receiving intimation from the depositor for the blocking of securities, the participant had informed the intermediary accordingly.

(iv) The participant of the intermediary had accordingly intimated the acceptance or rejection of deposit by the intermediary to the depository.

(v) In case the deposit was accepted by the intermediary, the depository had moved the securities from the lender’s account to the intermediary’s account and informed the participant of the lender.

(vi) The participant of the lender had accordingly intimated the lender about acceptance or rejection of his lending request.

(B) Lending of Securities by Intermediary to Borrower

To check that:

(i) A person who had desired to borrow securities under an approved securities lending program had made a request in the prescribed form to the participant.

(ii) DP had verified the request form for its validity and completeness and executed the instructions as per the specifications made in the form.

(iii) On execution of such instructions by the DP of the borrower, the depository had informed the DP of the intermediary accordingly.

(iv) DP of the intermediary had intimated the request for borrowing to the intermediary, which might have accepted or rejected the request.

(v) The acceptance or, as the case may be, rejection had been communicated to the DP in the prescribed form.
(vi) In case the request is accepted by the intermediary, the DP had informed the depository accordingly.

(vii) The participant of the borrower had informed the borrower about the acceptance or rejection by the depository of his request.

(C) Repayment of Securities by Borrower to Intermediary

To check that:

(i) A person who had desired to repay the securities borrowed under an approved security lending program made a request in the prescribed form to DP.

(ii) DP had verified the request form for its validity and completeness and executed the instructions as per the specifications made in the form.

(iii) Upon execution of the instructions, the securities proposed to be repaid were blocked by the depository in the borrower’s account in favour of the intermediary and intimation was sent to the participant of the intermediary.

(iv) The intermediary had submitted, in the prescribed form, his acceptance or, as the case may be, rejection of the repayment made by the borrower.

(v) In case the request is accepted by the intermediary, the DP had informed the depository accordingly.

(vi) The DP of the borrower had informed the borrower about acceptance or rejection of his request.

(vii) In case the borrower repaid the securities to the intermediary outside the securities lending module of DPM system, the DPs of the borrower, as well as the intermediary, had informed the depository accordingly.

(D) Recall of Securities by Intermediary from Borrower

If an intermediary who had lent securities under an approved securities lending program to a borrower had recalled the securities so lent, check that:

(i) The request for recalling had been made in the prescribed form through the DP.

(ii) The DP had verified the request form for its validity and completeness and executed the instructions as per the specifications made in the form.

(iii) After receiving intimation from the depository for the recall of securities, the DP of the borrower had informed the borrower accordingly.

(iv) The borrower on receipt of such intimation had conveyed his acceptance or rejection of the request for recall in the prescribed form to his DP.

(v) The DP of the borrower had informed the depository about the acceptance or, as the case may be, rejection of the request.

(vi) After receiving the intimation for acceptance/rejection of recall or securities from the depository, DP of the intermediary had informed the intermediary accordingly.

(vii) In case the intermediary had recalled the securities outside the securities lending module of DPM system, then DPs of the borrower had informed the
depository accordingly.

(E) Repayment of Securities by Intermediary to Lender

In the event an intermediary desired to return the securities received from a lender under an approved securities lending program, check that;

(i) The intermediary had made a request through its DP in the prescribed form.  
(ii) The DP had verified the request form for its validity and completeness and had executed the instructions as per the specifications made in the form.  
(iii) After receiving intimation from the depository for the blocking of securities, the DP of the lender had informed the lender accordingly.  
(iv) The lender had submitted, in the prescribed form, his acceptance or as the case may be, rejection of the repayment made by the intermediary.  
(v) The DP of the lender had accordingly intimated the acceptance or rejection of repayment by the intermediary to the depository.  
(vi) After receiving the intimation for acceptance/rejection of repayment of securities from the depository, the DP of the intermediary had informed the intermediary accordingly.  
(vii) In case the intermediary had repaid the securities to the lender outside the securities lending module of DPM system the DP of the lender had informed the depository accordingly.

(F) Recall of Securities by Lender from Intermediary

In case of a person who had lent securities through an approved intermediary and recalled the securities from the intermediary in accordance with the terms and conditions of the securities lending program and in the manner prescribed under bye-laws of the depository made in this regard check that:

(i) The lender had made the request for recalling the securities in the prescribed form through his DP.  
(ii) The DP had verified the request form for its validity and completeness and had executed the instructions as per the specifications made in the form.  
(iii) The DP of the intermediary had informed the intermediary accordingly.  
(iv) The intermediary on receipt of such intimation had submitted, in the prescribed form, his acceptance or, as the case may be, rejection of the recall request made by the lender.  
(v) DP, on receiving intimation of acceptance/rejection had intimated the depository accordingly.  
(vi) After receiving the intimation for acceptance/rejection of recall of securities from the depository, the DP of the lender had informed the lender accordingly.  
(vii) In case the lender recalls the securities from the intermediary outside the securities lending module of DPM system, DPs of the lender had informed the depository accordingly.
19. Furnishing and maintenance of Accounts

To check that:

(i) DP had furnished to the Depository every year, a copy of its audited financial statement and such report had been furnished not later than six months after the end of the DP’s financial year. Except where an extension of time to furnish such report has been granted.

(ii) DP had kept accounts and records in respect of the operations of the Depository distinct and independent from the records and accounts maintained by it in respect of any other activities carried out by the DP.

(iii) Proper accounts were maintained by the DPs in respect of the operations of the Depository in accordance with the software provided by the Depository.

(iv) The books of accounts and records of the DP relating to the operations of the Depository were open for inspection and audit to the officers of the Depository or their representatives. Such books of accounts and records were subjected to annual audit.

(v) DP had allowed persons authorised by the Depository to enter its premises during normal office hours and inspect its records relating to the operations of the Depository.

(vi) DP had submitted periodic returns to the Depository in the format specified by the Executive Committee or the Bye Laws or the Operating Instructions of the Depository, as the case may be.

20. Records to be maintained by the DPs

(A) DP had maintained the following records relating to its business for a period of five years in the case of NSDL and three years in the case of CDS:

(i) Delivery/Receipt Instruction given by its BOs.

(ii) Forms submitted by the BOs to the DP for:

(a) Opening of accounts with the DP, however in the case of active accounts the same cannot be destroyed;

(b) Closing of accounts with the DP;

(c) Freezing of accounts with the DP, however the same is to be maintained for five/three years or upto the time of defreezing whichever is later;

(d) Defreezing of accounts with the DP.

(iii) Copies of correspondence from the BOs on the basis of which BOs details were updated in the DPM;

(iv) Record of all actions taken on the exception reports, generated by the system;

(v) A register showing details of grievances received from the BOs and their present status. The following details may be specified in this regard:

(a) name of the BO;
(b) reference number of the BO;
(c) date;
(d) particulars of complaints;
(e) actions taken by the DP;
(vi) If the matter is referred to arbitration, then the particulars including the present status thereof;
(vii) Instructions received from the Clearing Member to transfer balances from the Pool account to the Delivery account of the Clearing Member in order to enable it to meet its obligations to the Clearing Corporation;
(viii) Instructions from the clearing member authorising the transfer of securities from the pool account of the clearing member to the accounts of its BOs;
(ix) The forms received in respect of pledge of securities;
(x) The forms received in respect of transmission of securities;
(xi) The Power of Attorney has been maintained till the account is active;
(xii) Forms received in respect of lending/borrowing of securities.

(B) The following records pertaining to dematerialisation and rematerialisation of securities were kept by the DPs until the process of dematerialisation or rematerialisation is completed:
(i) Dematerialisation request form (DRF) filled by the BO;
(ii) Certificate details of securities sent for dematerialisation;
(iii) Proof of deliveries of DRF and securities to the Issuer or its Registrar and Transfer Agent;
(iv) Objection memo and certificate details of the rejected securities against the DRN;
(v) Rematerialisation request form submitted by the BO;
(vi) Proof of delivery of RRF sent to the Issuer or its Registrar and Transfer Agent.

(C) The DP had intimated to the Depository, the place where the above records are kept and available for audit/inspection.

(D) The above requirements relating to maintenance of records apply not only to the records of the DP’s principal office but also any branch office and to any nominee company owned or controlled by the DP for the purpose of conducting the business of the DP relating to the operations of the Depository.

21. Disclosure/Publication of information

To ensure that DP does not by itself or through any other person(s) on its behalf publish, supply, show or make available to any other person or reprocess, retransmit, store or use any information provided by the Depository for any purpose other than in the ordinary course of its business as a user of the depository services, except with
the explicit approval of Depository.

**22. Supervision by DP**

To ensure that the DP:

(i) Establishes, maintains and enforces procedures to supervise its business and to supervise the activities of its employees, that are reasonably designed to achieve compliance with the Bye-Laws, Business Rules, Notifications and Directions issued thereunder by the Depository.

(ii) Maintains an internal record of the names of all persons who are designated as supervisory personnel and dates from which such designation is or was effective. Such records are/were preserved for a period of not less than three years.

(iii) Conducts a review, at least annually, of its business relating to operations of Depository, which is reasonably designed to assist in detecting and preventing violation of and achieving compliance of the Bye-Laws and Business Rules of the Depository.

(iv) Brings to the notice of its BOs, and other DPs, any indictments, penalties etc. imposed on it by Depository or any other regulatory authority within seven days from the date of such indictment or order.

(v) Brings to the notice of the Depository, any indictments or any other orders that may have been passed against it by any regulatory authority within 7 days from the date of such order or indictment.

(vi) Nominate a senior executive as Compliance Officer.

**23. Code of ethics for DPs**

The Business Rules of Depository provide the general principles and operational principles for Depository/DPs. The Business Rules of NSDL provide as under:

**(A) General principles**

(i) Professionalism: A DP in the conduct of its business shall observe high standards of commercial honour and just and equitable principles of business.

(ii) Adherence to Business Rules: DP shall adhere to the Bye-Laws and Business Rules of the Depository and shall comply with such operational parameters, rulings, notices, guidelines and instructions of the relevant authority as may be applicable from time to time.

(iii) Honesty and fairness : In conducting its business activities, a DP shall act honestly and fairly in the best interests of its BOs.

(iv) Capabilities: A DP shall have and employ effectively the resources and procedures which are needed for the proper performance of its business activities.

**(B) Operational Principles**

DPs shall ensure:
(i) That any employee who commits the DP to a transaction has the necessary authority to do so;

(ii) That employees are adequately trained in operating in the relevant areas they are assigned to and are aware of their own, and their organisation’s responsibilities as well as the relevant statutory Acts governing the DP, the Bye-Laws and the Business Rules including any additions or amendments thereof;

(iii) No DP or person associated with a DP shall make improper use of BO’s securities or funds.

(iv) While performing any transaction in the BO accounts, the DP must ensure that, great care is taken at all times not to misrepresent in any way, the nature of the transaction.

(v) No DP shall exercise any discretionary power in a BO’s account unless such BO has given prior written authorisation in this regard.

(C) General Guidelines

No DP shall shield or assist or omit to report about any DP whom it has known to have committed a breach or evasion of any Rules, Bye-laws, or Regulations of the Depository or of any resolution, order, notice or direction thereunder of the Executive Committee or the Managing Director or any committee or officer of the Depository authorised in that behalf.

24. Corporate Benefits

On information received from Depository the DP ensured that-

(i) Changes such as tax status, bank details, change of address, etc., in the beneficial owner accounts were updated well in advance of the record date/book closure.

(ii) In case of NSDL-DP there are no balances lying in the CM Accounts on the EOD of the record date or the EOD of one business day prior to the commencement of book closure. [However, CDSL considers all accounts as BO Accounts and any such balances are eligible for the Corporate benefits and it is not required to move the balances at the time of book closure].

(iii) It remains connected till the EOD of the record date or the EOD of one business day prior to the commencement of book closure.

25. Branch of Depository

All other branches of the DP offering depository services should be included for audit purpose. The internal auditor may consider ranking the branches on the basis of performance, compliance, and other operational related issues, stationery control, manpower planning, time management, etc. and other steps taken by the DP’s branches in helping the management to improve performance and ensure compliance of the standard operational procedures as stipulated in the Bye Laws, Business Rules, circulars, notices, directives, as may be issued from time to time by NSDL/CDS/SEBI.
Note: Although efforts have been made to give an exhaustive checklist, however, there could be circumstances requiring the auditor to check further items which he may deem necessary for the purpose of his audit.

**Guidelines for Dematerialisation of Shares Sent for Transfer by the Investors**

1. The issuer or its registrar and transfer agent shall on completion of the process of registration of shares submitted for transfer, intimate the investor providing an option to dematerialise such shares. The investor intending to exercise the option of dematerialising shares shall be required to send the Dematerialisation request within 15 days of the date of the option letter, failing which the issuer or its registrar and transfer agent shall proceed to despatch the share certificate.

2. Investors exercising the option (on receipt of a letter mentioned in 1 above) of dematerialising the shares shall submit the following documents to the participant:
   - Dematerialisation Request Form (DRF)
   - Original option letter received from the issuer or its registrar and Transfer Agent.

3. The words “as mentioned in the letter have already been” shall be inserted in place of the words “are hereby” on the client portion of the DRF.

4. The participant shall add the words “an option letter in respect of” after the words “We hereby acknowledge the receipt of” in the acknowledgement portion of the DRF and return the counterfoil of the DRF to the investor duly signed and stamped.

5. The participant shall add the words “option letter in respect of” after the words “The application form is verified with the” and replace the words “option letter” in place of the word “certificate” on the participant Authorisation portion of the DRF.

6. The participant shall affix its seal and signature on the original option letter.

7. The participant shall execute the request for Dematerialisation in the depository participant module (DPM).

8. The participant shall forward such details of the certificate of security to the depository and shall confirm to the depository that an agreement has been entered between the participant and the beneficial owner.

9. The participant shall maintain records indicating the names of beneficial owners of the securities surrendered, the number of securities and other details of the certificate of security sent for dematerialisation.

10. The participant shall despatch the DRF along with the original option letter to the issuer or its registrar and transfer agent and keep a copy thereof for its records.

11. The issuer or its registrar and transfer agent shall process the
dematerialisation request for its validity and verify the signature(s) on the DRF with the signature(s) on the transfer deed.

12. If the request is in order, the issuer or its registrar and transfer agent shall deface the certificates with the words “Dematerialised” and then confirm the dematerialisation request.

13. The issuer or its registrar and transfer agent shall substitute in its records the name of the depository as the registered owner and shall send a certificate to the depository and to every stock exchange where the security is listed.

14. Immediately upon the receipt of information from the issuer or its registrar and transfer agent regarding confirmation of dematerialisation, the depository shall enter in its records the name of the person who has surrendered the certificate of security as the Beneficial Owner, as well as the name of the participant from whom it has received intimation under point 8 and shall sent an intimation of the same of participant.

15. The issuer or its registrar and transfer agent shall maintain a record of certificates of securities which have been dematerialised.

16. If the request is rejected, the issuer or its registrar and transfer agent shall despatch the certificates to the investor.

17. NSDL shall obtain from the company a certificate certified by a Chartered Accountant or a Company Secretary holding a Certificate of Practice that the company has followed the above procedure and to the following effect:

   — The Company has followed the necessary procedure for effecting the original transfer.

   — The Register of Members of the company was accordingly amended and the shares were transferred in favour of the transferee.

   — The company has adequate procedure and has satisfied itself that the transferee and the entity requesting for dematerialisation are one and the same and before confirming the dematerialisation request, the company has further amended its register of members to indicate the transfer from the transferee to NSDL.

   — The company has defaced and cancelled/mutilated all the certificates.

   — The company has adequate systems to ensure that the investor does not lose his corporate benefits on account of the transfer entries made in favour of NSDL.


1. Check whether DPs have formulated policy framework in keeping with the objectives of Anti Money Laundering Measures.

2. Whether they have designated an officer as ‘principal offer” who should be responsible for compliances under PMLA.
3. Whether Depository Participants are adhering to the guidelines especially with reference to:
   1. Customer due diligence identification and acceptance
   2. Record keeping
   3. Monitoring & Reporting of cash/suspicious transactions
   4. Risk-based approach.

4. Whether the DPs are prompt in reporting cash/suspicious transactions to Financial Intelligence Unit – India.

CONCURRENT AUDIT

National Securities Depository Limited vide its Circular No. NSDL/POLICY/2006/0021 dated June 24, 2006 provides for concurrent audit of the Depository Participants. The Circular provides that w.e.f. August 1, 2006, the process of demat account opening, control and verification of Delivery Instruction Slips (DIS) is subject to Concurrent Audit. Depository Participants have been advised to appoint a firm of qualified Chartered Accountant(s) or Company Secretary(ies) holding a certificate of practice for conducting the concurrent audit. However, the participants in case they so desire, may entrust the concurrent audit to their Internal Auditors.

The Concurrent Auditor should conduct the audit in respect of all accounts opened, DIS issued and controls on DIS as mentioned above, during the day, by the next working day. In case the audit could not be completed within the next working day due to large volume, the auditor should ensure that the audit is completed within a week’s time.

Any deviation and/or non-compliance observed in the aforesaid areas should be mentioned in the audit report of the Concurrent Auditor. The Management of the Participant should comment on the observations made by the Concurrent Auditor.

LESSON ROUND-UP

- Just like a broker who acts as an agent of the investor at the Stock Exchange; a Depository Participant (DP) is the representative (agent) of the investor in the depository system providing the link between the Company and investor through the Depository.

- The two Depository service provides in India, viz., National Securities Depository Ltd. (NSDL) and Central Depository Services (India) Limited (CDS) have allowed Company Secretaries in whole-time Practice to undertake internal audit of the operations of Depository Participants (DPs).

- The depository business in India is regulated by –
  - The Depositories Act, 1996
  - The SEBI (Depositories and Participants) Regulations, 1996
  - Bye-laws of Depository
Internal Audit of depository participants broadly covers the following areas:
2. Dematerialisation/Rematerialisation.
3. Dealing with B.Os.
4. Regulatory Compliances.
5. Transfer/transmission.
6. Internal Control etc.

SELF-TEST QUESTIONS
(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation.)
1. State the role of Depository Participants (DPs).
2. Describe the scope and objectives of Internal Audit of Depository Participants.
3. Describe the terms ‘Corporate Action’, Dematerialisation and ‘rematerialisation’
4. Describe the procedure for conducting internal audit of depository participants.
The objective of this study lesson is to enable the students to understand

- Concept and types of Depositary Receipts
- Sponsored Global Depositary Receipts/Global Depositary Receipts through Fresh issue of shares
- Regulatory framework in and outside India in respect of issue of GDRs
- Parties, documents, approvals and process involved in the issue of GDRs
- Check list for issue of Global Depositary Receipts/American Depositary Receipts

I. INTRODUCTION

The Government has taken a number of policy initiatives to allow Indian companies to raise resources from the International markets. Consequently raising funds through Euro Issues has become popular with Indian companies and investors both. Indian companies found this route very attractive and today more and more companies are trying this avenue to raise funds. International offering made by companies for tapping the international capital markets can be through the following modes.
Foreign Currency Convertible Bond, is an Equity-linked convertible security that can be converted/exchanged for a specific number of shares of the issuer company.

Depositary Receipts (DRs) are negotiable securities issued outside India by a Depositary Bank, on behalf of an Indian company, which represent the local Rupee denominated equity shares of the company held as deposit by a Custodian Bank in India. DRs are traded in Stock Exchanges in the US, Singapore, Luxembourg etc. DRs listed and traded in the US markets are known as American Depositary Receipts (ADRs) and those listed and traded elsewhere are known as Global Depositary Receipts (GDRs). In the Indian context, DRs are treated as FDI. Indian companies can raise foreign currency resources abroad through the issue of ADRs/GDRs, in accordance with the Scheme for issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depositary Receipt Mechanism) Scheme, 1993 and guidelines issued by the Central Government there under from time to time.

Exchange traded depository receipts from India have been relatively recent phenomenon (i.e. late 90’s) though few companies have issued GDRs through private placement in early 90’s. At present these are several active depository receipts such as Satyam, Infosys, ITC, Dr. Reddys, L&T etc. that are listed either on American exchanges like the Newyork Stock Exchange or NASDAQ or on European/Asian exchanges such as London, Dubai, Singapore exchanges. Reliance Industries was the first Indian company to be listed on NYSE and Infosys was the first Indian company to be listed on NASDAQ.

II. TYPES OF DEPOSITARY RECEIPTS

1. American Depositary Receipts (ADRs)

An American Depositary Receipt (“ADR”) is a dollar denominated form of equity ownership in the form of depositary receipts in a non-US company. It represents the foreign shares of the company held on deposit by a custodian bank in the company’s home country and carries the corporate and economic rights of the foreign shares.

Following are the types of ADRs

(a) Level I ADR (unlisted, OTC traded/Pink Sheets)

This is the least expensive level to provide for issuance of shares in ADR form in the US. The company issuing ADRs has to comply with the SEC registration requirements but can be exempted from full SEC reporting requirements under certain circumstances. It can only be traded over-the-counter and cannot be listed on a national exchange in the US. The electronic OTC markets are also called pink sheets which is a centralized quotation service that collects and publishes market maker quotes for OTC securities in real time.

(b) Level II ADRs (US Listed, Non-capital Raising Transaction (i.e. without going for public issue)

This programme gives more liquidity and marketability as it enables listing of ADRs in one or more of the US exchanges. Under this programme the company has to comply with the registration requirements, reporting requirements of SEC.
(c) Level III ADRs (US listed Capital Raising Transaction i.e., through fresh issue of shares) – This type of ADRs which are to comply with SECA Registration, Reporting requirement and after document filing.

(d) Rule 144A Depositary Receipts (Privately placed for QIBs and cannot be bought on the public exchanges or over the counter.)

2. Global Depositary Receipts

GDRs have access usually to Euro market and US market.

GDRs are often launched for capital raising purposes, so the US element is generally either through Rule 144(a) ADR or a Level III ADR, depending on whether the issuer aims to tap the private placement or public US markets.

The US portion of GDRs to be listed on US exchanges to comply with SEC requirements and the European portion are to be complied with EU directive.

(a) Listing of Global Depositary Receipts

Listing of GDR may take place in international stock exchanges such as London Stock Exchange, New York Stock Exchange, American Stock Exchange, NASDAQ, Luxemburg Stock Exchange etc.

International investors are interested in diversifying their portfolio across their national borders either through direct investment or through investment in depositary receipts from the exchanges of their home country. Investment in depositary receipts is an easier route for a small/medium investor. Through listing of depositary receipts in foreign exchanges, foreign investors gain benefits of diversification of portfolio while trading in their market under their own settlement and clearance process.

(b) Sponsored GDRs Vs GDRs through fresh issue of shares

GDR issue can be through sponsored GDR programme or through fresh issue of shares.

Through Sponsored GDRs the existing holders of shares in Indian Companies can sell their shares in the overseas market. It is a process of disinvestment by Indian shareholders of their holding in overseas market. The concerned Company sponsors the GDRs against the shares offered for disinvestment. These shares are converted into GDRs and sold to foreign investors. The proceeds realized are distributed to the shareholders in proportion to the shares sold by them.

For the benefit of Indian shareholders, RBI has amended Issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993 ('the Scheme'), to enable such shareholders to sell their shares in overseas markets, by way of Sponsored ADRs/GDRs.

Scheme of Sponsored ADRs/GDRs

Paragraph 4B of the Scheme provides that—
(i) An Indian company may sponsor an issue of ADRs/GDRs with an overseas depository against shares held by its shareholders at a price to be determined by the Lead Manager.

(ii) The proceeds of the issue shall be repatriated to India within a period of one month.

(iii) The sponsoring company shall comply with the provisions of the Scheme and guidelines issued in this regard by the Central Government from time to time.

(iv) The sponsoring company shall furnish full details of such issue, in the form specified under Annexure C to the Scheme, to the Foreign Investment Division, Exchange Control Department, Reserve Bank of India, Central Office, Mumbai within 30 days from the date of closure of the issue.

In a layman’s language, the Scheme of Sponsored ADRs/GDRs is a process of disinvestments by the Indian shareholders of their holdings in overseas markets. The concerned company sponsors the ADRs/GDRs against the shares offered for disinvestments. Such shares are converted into ADRs/GDRs according to a pre-fixed ratio and sold to overseas investors. The proceeds realized are distributed to the shareholders in proportion to the shares sold by them.

Example

Say, a company sponsors 1 million equity shares to be converted into 2 million GDRs (ratio of course depends on the existing market price of shares and GDRs). Shareholders, as on the record date fixed for the purpose, tender their shares in the offering. If the shares offered for sale are more than the prespecified number, in our example it is 1 million shares would be accepted pro-rata. The accepted shares are then converted into GDRs and sold to overseas investors. The sale proceeds, after meeting with the issue expenses, are distributed to the shareholders proportionately.

(c) Two-way Fungibility of GDRs

A limited Two-way Fungibility scheme has been put in place by the Government of India for ADRs / GDRs. Under this scheme, a stock broker in India, registered with SEBI, can purchase shares of an Indian company from the market for conversion into ADRs/GDRs based on instructions received from overseas investors. Re-issuance of ADRs /GDRs would be permitted to the extent of ADRs / GDRs which have been redeemed into underlying shares and sold in the Indian market.

III. BROAD REGULATORY FRAMEWORK WITHIN AND OUTSIDE INDIA ON ISSUE OF DEPOSITARY RECEIPTS

1. Indian Regulatory Framework in respect of issue of GDR

(a) Foreign Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme 2003.

Global Depositary Receipts in India are made under Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993 and guidelines issued by the Central Government there under from time to time. The important features of the amended scheme are as under

— Companies issuing GDRs do not require approval of Ministry of Finance
— GDR issue shall not exceed the sectoral cap of FDI policy. If so FIPB approval is to be obtained.
— Indian companies restrained by SEBI from raising capital, is not eligible to issue GDRs
— Indian companies issuing GDRs has to comply with the specified pricing norms.
— Unlisted companies floating GDRs has to get its shares simultaneously listed in Indian exchange/s.
— The proceeds of the issue cannot be used for investing in the stock market or real estate.
— The issue expenses shall not exceed the specified limit.
— The company has to comply with the reporting requirements of RBI.

(b) Listing Agreement
As FCCB and Ordinary Shares (Through Depository Receipt Mechanism) Scheme 2003 requires unlisted companies floating GDRs, to get its shares simultaneously listed in Indian exchanges, with respect to underlying shares of the company issuing GDRs, all provisions on listing agreement and other filings with the stock exchanges in India has to be complied with.

(c) Companies Act, 1956
— The underlying shares are to be offered to more than 50 people, as it is a public offer [Section 67(3)]
— Filing of Prospectus with ROC (Section 60).

(d) SEBI (DIP) Guidelines, 2000
Though it is not applicable to GDRs as such, simultaneous listing of shares of unlisted companies floating GDRs, are to comply with SEBI (DIP) Guidelines, 2000.

2. Regulatory framework outside India
(a) SEC requirements for issue of Global Depositary Receipts in America
As discussed earlier, Global Depositary Receipts may be listed either at exchanges based at Europe or at America. Accordingly American Depositary Receipts and Global Depositary Receipts issued/proposed to be listed at US-exchanges are required to comply with SEC requirements.

A non-US company (say an Indian Company) to be able to sell its’ DRs representing its shares into the United States, it must either be a “reporting company” under the United States Exchange Act of 1934 or be exempt from such reporting requirements.

An exemption from the reporting requirements of the is provided for under Rule 12g3(2)-b of the Act to level I ADRs (i.e. unlisted, OTC Trade Depository Receipts) and rule 144A depositary receipts (i.e. depository receipts through private placement). In order to obtain the exemption, the company must apply to the United States Securities and Exchange Commission, through an application which has to provide information about the number of holders of each class of equity securities who are U.S. residents, the amount and percentage of each such class that U.S. residents hold and the circumstances in which they acquired such securities etc
The following are the important compliance requirements with SEC, based on the type of depositary Receipts.

**Form F-6 – Registration of depositary shares evidenced by GDRs/ADRs**

Form F-6 is used for the registration of depositary shares as evidenced by DRs that are issued by a depository bank against the deposit of securities of an Indian Company. The information is prepared by the company under the guidance of the depository bank at the inception of either an unsponsored or sponsored program.

**Form 6K**

Form 6k is to be filed with securities exchange commission by a foreign private issuer, pursuant to rule 13a-16 or 15d-16 under the securities exchange act of 1934 to provide information that is required to be made public in the country of its domicile.

**Form 20-F – Report on material business activities**

A Form 20-F is a comprehensive report of all material business activities and financial results and must comply with US GAAP. It has four distinct parts.

- **Part I** requires a full description of the issuer’s business, details of its property, any outstanding legal proceedings, taxation and any exchange controls that might affect security holders.
- **Part II** requires a description of any securities to be registered, the name of the depositary bank for the GDRs and all fees to be charged to the holders of GDRs.
- **Part III** requires information on any defaults upon securities, and
- **Part IV** requires various financial statements to be submitted.

This reporting requirement is essential when the company desires to list its securities in the US exchange through sponsored program or fresh issue.

**Form F-1 – Filing of information to be included in the prospectus**

Indian Companies planning a public offering in the US and wants to gets its securities on US exchange has to register its securities in Form F-1. This form requires certain information to be included in the prospectus such as use of proceeds, summary information, risk factors and ratio of earnings to fixed charges, determination of offering price, dilution, plan of distribution, description of securities to be registered, name of legal counsel and disclosure of commissions etc.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Level I ADR</th>
<th>Level II ADR</th>
<th>Level III ADR</th>
<th>Private Placement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Listing</td>
<td>Unlisted programme/OTC traded (called Pink Sheets)</td>
<td>Listed on US exchange</td>
<td>Shares offered and listed on US exchange</td>
<td>Issued to QIBs (i.e. Rule 144A)</td>
</tr>
<tr>
<td>SEC compliance</td>
<td>Registration under form F-6 and exempted from reporting</td>
<td>Registration in form 6 and to comply with reporting requirements</td>
<td>Registration under form F-6, Reporting under form 20-F and</td>
<td>None</td>
</tr>
</tbody>
</table>
(b) Compliance under EU directive in respect of issue of Global Depositary Receipts

For issue of GDRs being listed in European exchanges has to comply with Prospectus directive, Transparency obligations directive and Market Abuse Directive issued by EU and also country specific laws.

**Prospectus directive**


The Prospectus Directive (PD) sets out the initial disclosure obligations for issuers of securities that are offered to the public or admitted to trading on a regulated market in the EU. It provides a passport for issuers that enable them to raise capital across the EU on the basis of a single prospectus.

**Transparency obligations directive**

It requires issuers to make certain periodic disclosures including annual, half yearly reports etc.

**Market Abuse Directive**

The Market Abuse Directive aims at tackling insider dealing and market manipulation in the EU and the proper disclosure of information to the market. It requires immediate disclosure of price-sensitive information by issuers of securities which are admitted to an EU market

IV. PARTIES, APPROVALS, DOCUMENTATION AND PROCESS INVOLVED IN THE ISSUE OF GDRs

1. Parties involved

The following agencies are normally involved in the Euro issue:

(i) Lead Manager (ii) Co-Lead/Co-Manager (iii) Overseas Depositary Bank (iv) Domestic Custodian Banks (v) Listing Agent (vi) Legal Advisors (vii) Printers (viii) Auditors (ix) Underwriter

(a) Lead Manager

The company has to choose a competent lead manager to structure the issue and arrange for the marketing. Lead managers usually charge a fee as a percent of the issue. The issues related to public or private placement, nature of investment, coupon rate on bonds and conversion price are to be decided in consultation with the lead manager.

(b) Co-Lead/Co-Manager

In consultation with the lead manager, the company has to appoint co-lead/co-
manager to coordinate with the issuing company/lead manager to make the smooth launching of the Euro issue

(c) *Overseas Depositary Bank*

It is the bank which is authorised by the issuing company to issue Depositary Receipts against issue of ordinary shares or Foreign Currency Convertible Bonds of issuing company.

(d) *Domestic Custodian Bank*

This is a banking company which acts as custodian for the ordinary shares or Foreign Currency Convertible Bonds of an Indian company, which are issued by it. The domestic custodian bank functions in co-ordination with the depositary bank. When the shares are issued by a company the same are registered in the name of depositary and physical possession is handed over to the custodian. The beneficial interest in respect of such shares, however, rests with the investors.

(e) *Listing Agent*

One of the conditions of Euro-issue is that it should be listed at one or more Overseas Stock Exchanges. The appointment of listing agent is necessary to coordinate with issuing company for listing the securities on Overseas Stock Exchanges.

(f) *Legal Advisors*

The issuing company should appoint legal advisors who will guide the company and the lead manager to prepare offer document, depositary agreement, indemnity agreement and subscription agreement.

(g) *Printers*

The issuing company should appoint printers of international repute for printing Offer Circular.

(h) *Auditors*

The role of issuer company’s auditors is to prepare the auditors report for inclusion in the offer document, provide requisite comfort letters and reconciliation of the issuer company’s accounts between Indian GAAP/UK GAAP/US-GAAP and significant differences between Indian GAAP/UK GAAP/US.

(i) *Underwriters*

It is desirable to get the Euro issue underwritten by banks and syndicates. Usually, the underwriters subscribe for a portion of the issue with arrangements for tie-up for the balance with their clients. In addition, they will interact with the influential investors and assist the lead manager to complete the issue successfully.

2. *Approvals involved*

(a) *Approval of Board of Directors*

A meeting of Board of Directors is required to be held for approving the proposal to raise money from Euro Capital market. The resolution should indicate therein
specific purposes for which funds are required, quantum of the issue, country in
which issue is to be launched, time of the issue etc. The Board meeting shall also
decide and approve the notice of Extraordinary general meeting of shareholders at
which special resolution is to be considered.

(b) Approval of Shareholders

Proposal for making Euro issue, as proposed by Board of Directors require
approval of shareholders.

A special resolution under Section 81(1A) of the Companies Act, 1956 is required
to be passed at a duly convened general meeting of the shareholders
of the company. Approvals under Sections 94, 16 and 31 of the Companies Act, 1956
may also be obtained, if required. Form No. 23 along with requisite filing fee is to be
filed with ROC of the State in which the registered office of the company is situated.

(c) Approval of Department of Company Affairs

Approval as to compliance of Section 187C, non-applicability of provisions
relating to prospectus and Section 108 for transfer of shares is also sought for.

(d) Post facto Approval of Reserve Bank of India

The issuer company has to obtain approvals from Reserve Bank of India under
circumstances specified under the guidelines issued by the concerned authorities
from time to time.

RBI vide its press release dated January 20, 2000 granted general permissions
to make an international offering of rupee denominated equity shares of the company
by way of issue of ADR/GDR.

(e) In-principle consent of Stock Exchanges for listing of underlying shares

The issuing company has to make a request to the domestic stock exchange for
in-principle consent for listing of underlying shares which shall be lying in the custody
of domestic custodian. These shares, when released by the custodian after
cancellation of GDR, are traded on Indian stock exchanges like any other equity
shares

(f) In-principle consent of Financial Institutions

Where term loans have been obtained by the company from the financial
institutions, the agreement relating to the loan contains a stipulation that the consent
of the financial institution has to be obtained. The company must obtain in-principle
consent on the broad terms of the proposed issue.

(g) Approval of FIPB in certain cases

As GDR is considered as Foreign Direct Investments, the GDR issue exceeding
the limits specified under FDI policy, requires approval of FIPB.

3. Documentation involved
The following principal documents are involved in the issue of GDRs:

(i) Subscription Agreement
(ii) Depositary Agreement
(iii) Custodian Agreement
(vi) Listing Agreement
(vii) Information Memorandum
(viii) SEC Registration/Reporting and Exemptions

(a) Subscription Agreement

Subscription agreement provides that Lead Managers and other managers agree, severally and not jointly, with the company, subject to the satisfaction of certain conditions, to subscribe for GDRs at the offering price set forth. It may provide that obligations of managers are subject to certain conditions precedent.

(b) Depositary Agreement

Depositary agreement lays down the detailed arrangements entered into by the company with the Depositary, the forms and terms of the depositary receipts which are represented by the deposited shares.

(c) Custodian Agreement

Custodian works in co-ordination with the depositary and has to observe all obligations imposed on it including those mentioned in the depositary agreement. The custodian is responsible solely to the depositary. In the case of the depositary and the custodian being same legal entity, references to them separately in the depositary agreement or otherwise may be made for convenience and the legal entity will be responsible for discharging both functions directly to the holders and the company.

Listing Agreement

Listing agreement is an agreement with the concern stock exchange in which the company has proposed to list its GDRs.

SEC Registration/Exemption

It covers registration documents in form F-6, form for registration of securities in form F-1 and F-6 for registration and

4. Process involved in the issue of GDRs

Following are the broad steps involved in GDR issue

1. Indian company would issue rupee denominated shares to a depositary outside India, where the GDRs are proposed to be issued.
2. Indian custodian would keep these securities in his custody.
3. The investment banker would organize road shows for marketing the issue.
4. The foreign Depositary would issue dollar denominated GDRs to foreign investors.
5. Listing of GDRs in American and European Stock Exchanges would take place.
6. Indian company has to comply with various requirements of EU directives and SEC requirements.

The following flowchart explains the issue of GDRs.

In case of sponsored GDRs, the process involved would be as follows.

V. CHECK-LIST IN RESPECT OF DUE DILIGENCE OF ISSUE OF GLOBAL DEPOSITARY RECEIPTS

1. Eligibility of issuer

Check whether the company is eligible to access the capital market and not been restrained by SEBI from accessing capital market.

It may be noted that an Indian Company, which is not eligible to raise funds from the Indian Capital Market including a company which has been restrained from
accessing the securities market by the Securities and Exchange Board of India (SEBI) will not be eligible to issue (i) Foreign Currency Convertible Bonds and (ii) Ordinary Shares through Global Depositary Receipts under the Foreign Currency Convertible Bonds and Ordinary Shares (Through Depositary Receipt Mechanism) Scheme, 1993.

2. Eligibility of subscriber

Check whether any erstwhile Overseas Corporate Bodies (OCBs) who are not eligible to invest in India through the portfolio route and entities prohibited to buy, sell or deal in securities by SEBI, have not subscribed.

It may be noted that erstwhile Overseas Corporate Bodies (OCBs) who are not eligible to invest in India through the portfolio route and entities prohibited to buy, sell or deal in securities by SEBI will not be eligible to subscribe to (i) Foreign Currency Convertible Bonds and (ii) Ordinary Shares through Global Depositary Receipts under the Foreign Currency Convertible Bonds and Ordinary Shares (Through Depositary Receipt Mechanism) Scheme, 1993.

3. Limits of foreign investment in the issuing company

The ordinary shares and FCCBs issued against the GDRs shall be treated as FDI and the aggregate of the foreign investment made either directly or indirectly (through Depository Receipts Mechanism) shall not exceed 51% of the issued and subscribed capital of the issuing company. However, the investments made through offshore funds or by FII will not form part of the said limits.

4. Simultaneous listing in India

(i) Check whether the unlisted company issuing GDR has simultaneously listed its securities in India.

(ii) Check whether the company has complied with rule 19(2)(b) of Securities Contracts (Regulation) Rules, 1957 regarding requirement of minimum public offering.

(iii) Check whether the company has complied with the SEBI(DIP) Guidelines in respect of public offer made for the purpose of domestic listing.

It may be noted that unlisted companies, which have not yet accessed the Global Depositary Receipt / Foreign Currency Convertible Bond route for raising capital in the international market would require prior or simultaneous listing in the domestic market, while seeking to issue (i) Foreign Currency Convertible Bonds and (ii) Ordinary Shares through Global Depositary Receipts under the Foreign Currency Convertible Bonds and Ordinary Shares (Through Depositary Receipt Mechanism) Scheme, 1993.

Further unlisted companies, which have already issued Global Depositary Receipts/Foreign Currency Convertible Bonds in the international market, would now require to list in the domestic market on making profit beginning financial year 2005-06 or within three years of such issue of Global Depositary Receipts/Foreign Currency Convertible Bonds, whichever is earlier.

5. Pricing
Listed Companies

Check whether the pricing of Global Depositary Receipt is made at a price not less than the higher of the following two averages:

(i) The average of the weekly high and low of the closing prices of the related shares quoted on the stock exchange during the six months preceding the relevant date;

(ii) The average of the weekly high and low of the closing prices of the related shares quoted on a stock exchange during the two weeks preceding the relevant date.

The “relevant date” means the date thirty days prior to the date on which the meeting of the general body of shareholders is held, in terms of section 81 (IA) of the Companies Act, 1956, to consider the proposed issue.

Unlisted Companies

Check whether the price is arrived at in consultation with the Lead Manager to the issue, in case where the GDR issue is on public offer basis

Check whether the price is not less than the fair valuation of shares done by a Chartered Accountant as per the guidelines issued by the Erstwhile Controller of Capital issues.

6. Issue Expenses

Check whether the issue related expenses (including legal expenses, lead manager charges, underwriting commission etc) has not exceeded 4% in case of non-listed GDRs and 7% in case of GDRs listed on US exchange.

7. Companies Act requirements

Check whether the company has passed a special resolution under Section 81(1A) of the Companies Act, 1956 at a duly convened general meeting of the shareholders of the company in respect of GDR issue.

Check whether the company has altered Capital clause of Memorandum of Association and filed necessary forms with Registrar of Companies, if the authorized capital of the company is likely to be increased after GDR issue

Check whether the company has passed necessary special resolution, if the GDR issue has resulted in alteration of Articles of Association

8. FEMA requirements

Check whether the GDRs issued are within the limits specified in the FDI policy? If not check whether FIPB approval has been obtained?

9. SEC Registration/Exemption/reporting requirements

Check whether the company has filed Registration under form F-6, Reporting under form 20-F and registration of securities proposed to be offered in form F-1 with
the Securities and Exchange Commission.

10. EU Directives in respect of issue of GDRs

Check whether the company has complied with Prospectus directive, Transparency obligations directive and Market Abuse Directive issued by EU.

11. RBI Reporting

Check whether the company has reported the necessary information such as number/amount of GDRs, number of underlying Indian security, amount of foreign capital on account of GDRs etc within 30 day of completion of GDR issue.

12. Disinvestment in case of Sponsored GDRs

(a) Check whether the company has passed special resolution for disinvestment of existing shares in GDR market

(b) Check whether the GDRs issued against disinvestment of existing shares would come within the purview of SEBI Takeover code.

(c) Check whether the approval of FIPB is obtained if required?

(d) Check the shares earmarked for the sponsored GDR was kept in an escrow account and such retention in escrow account has not exceeded 3 months.

(e) Check whether the proceeds of GDR issue raised abroad is repatriated to India within one month of the closure of the issue.

(f) Check the necessary information such as amount and number of GDRs, Percentage of foreign capital after disinvestment, details of repatriation etc is furnished to the exchange control department of RBI, Mumbai within 30 days of completion of such transaction.

13. Transfer and redemption

(a) Check whether necessary RBI permission has been obtained in respect of transfer of depository receipts to a resident as underlying shares.

(b) Check whether re-issue of redeemed GDRs have complied with FEM (Transfer or Issue of Security by a person Resident Outside India) Regulations, 2000.

LESSON ROUND-UP

- Global Depositary Receipts means any instrument in the form of a Depositary receipt or certificate (by whatever name it is called) created by the Overseas Depositary Bank outside India and issued to non-resident investors against the issue of ordinary shares or Foreign Currency Convertible Bonds of issuing company
- Domestic Custodian Bank means a banking company which acts as a custodian for the ordinary shares or foreign currency convertible bonds of an Indian Company which are issued by it against global Depositary receipts or certificates
- Overseas Depositary Bank means a bank authorised by the issuing company to issue global Depositary receipts against issue of Foreign Currency Convertible
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<tr>
<td>• Indian Companies issuing GDRs in America and Europe has to comply with SEC requirements and EU directives.</td>
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</table>

**SELF-TEST QUESTIONS**

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. What are the various options for a company issuing Global Depositary Receipts?
2. Describe the SEC requirements in respect of GDRs proposed to be listed in US exchanges?
3. Write short notes on
   (a) Pink Sheets
   (b) Domestic Custodian Bank
   (c) Overseas Depositary
4. What are the provisions relating to transfer/redemption of GDRs?
5. Describe the working mechanism of GDRs?
6. What are the check list in respect of due diligence of GDR issue?
STUDY VIII
INDIAN DEPOSITORY RECEIPTS

LEARNING OBJECTIVES

The objective of this study lesson is to enable the students to understand

• Concept of Indian Depository Receipts
• Regulatory Framework for issue of Indian Depository Receipts
• Procedures for making an issue of Indian Depository Receipts
• Checklist for issue of Indian Depository Receipts (IDRs) under
  (a) Companies (Issue of Indian Depository Receipts) Rules, 2004
  (b) Chapter VI A of SEBI (DIP) Guidelines, 2000
  (c) Listing Agreement for IDRs

I. INTRODUCTION

Investment in Indian Depository Receipts (IDRs) is an interesting opportunity for the Indian Investors who are looking for investing their funds in foreign equity. Just like American Depository Receipts or Global Depository Receipts, which are instruments used by Indian Companies to raise money abroad, IDRs are meant for foreign companies looking to raise capital in India.

Indian Depository Receipt means any instrument in the form of a depository receipt created by Domestic Depository in India against the underlying equity shares of issuing company which is located outside India. The Indian IDR holders would thus indirectly own the equity shares of overseas issuer company. IDRs are to be listed and denominated in Indian Currency. An issuing company cannot raise funds in India by issuing IDRs unless it has obtained prior permission from SEBI.

The parties involved in the issue of Indian Depositary Receipts are:

(a) Issuing Company (Foreign Company)
(b) Overseas Custodian (custodian located at the same country where issuing company is located).
(c) Domestic Depository (Depositary located in India)
(d) Indian Investors who has invested in IDR issue

Accordingly to Companies (Issue of Indian Depository Receipts) Rules, 2004,

“Issuing company” means a company incorporated outside India, making an issue of IDRs through a domestic depositary;

“Overseas Custodian Bank” means a banking company which is established in a country outside India and which acts as custodian for the equity shares of Issuing Company, against which IDRs are proposed to be issued by having a custodial arrangement or agreement with the Domestic Depository or by establishing a place of
business in India.

Overseas Custodian bank can act as a custodian by
— having a custodial arrangement or
— agreement with the Domestic Depository or
— establishing a place of business in India.

“Domestic Depository” means custodian of securities registered with SEBI and authorised by the issuing company to issue Indian Depository Receipts.

The following flow chart explains the IDR process

II. BROAD REGULATORY FRAMEWORK IN RESPECT OF ISSUE OF IDRS

Issue of Indian Depository Receipts are mainly regulated by


The Central Government vide its powers conferred by clause (a) of sub-section (1) of section 642 read with section 605A of the Companies Act, 1956, notified Companies (Issue of Indian Depository Receipts) Rules, 2004. These rules are applicable only to those companies incorporated outside India, whether they have or have not established any place of business in India.

Salient Features of these rules are:
— It prescribes eligibility of an issuing company with respect to paid-up capital, free reserves, profits, debt-equity ratio etc.
— It specifies broad procedure for an issue of IDRs with respect of filing of
documents with SEBI, listing permission with stock exchanges etc.
— It imposes certain condition for issue of IDRs such as maximum percentage of IDRs permissible on paid up capital & reserves, repatriation of proceeds out of redemption of IDRs, issue of prospectus and application etc.
— It describes the procedure for registration of document with SEBI and ROC by Merchant Banker.
— It has clauses relating to disclosure requirements, distribution of corporate benefits etc.
— It prescribes procedure for transfer or redemption of IDRs
— It requires issuing company to make quarterly disclosures on utilization of funds raised through issue of IDRs. This disclosure has to be made to Overseas Custodian Bank and Domestic Depository and has also to be published in one English newspaper having wide circulation in India.
— It has a schedule with respect to matters to be specified in the prospectus.

(b) Chapter VI A of SEBI (DIP) Guidelines, 2000

Chapter VI A of SEBI (Disclosure of Investor Protection) Guidelines 2000 deal with issue of Indian Depository Receipts. The guidelines given in this Chapter are in addition to the provisions of the Companies (Issue of Indian Depository Receipts) Rules, 2004. It also contains clauses pertaining to eligibility of issuer, minimum application amount, investment limits for investors, minimum subscription, prospectus disclosures etc.

(c) Listing agreement for IDRs

Every issuer of an IDR has to comply with the conditions stipulated in the listing agreement for IDRs issued by SEBI. The highlights of the same are enumerated in the table which is enclosed as Annexure A.

III. CHECKLIST IN RESPECT OF ISSUE OF INDIAN DEPOSITORY RECEIPTS

(a) Checklist under Companies (Issue of Indian Depository Receipts) Rules, 2004

1. Eligibility for issue of IDRs (Rule 4)

   (a) Check whether pre- issue paid-up capital and free reserves are at least US$ 50 million and it has a minimum average market capitalization (during the last 3 years) in its parent country of at least US$ 100 million;

   (b) Check whether it has a continuous trading record or history on a stock exchange in its parent country for at least three immediately preceding years;

   (c) Check whether it has a track record of distributable profits in terms of Section 205 of the Companies Act, 1956, for at least three out of immediately preceding five years;

   (d) Check whether it fulfills such other eligibility criteria as may be laid down by Securities and Exchange Board of India (SEBI) from time to time in this behalf.

2. Procedural matters
(a) Check whether the issuing company has obtained prior permission from the SEBI for issuing IDRs.

(b) Check whether the application seeking an issue of IDR has been made to the SEBI at least 90 days prior to the opening date of the issue along with non-refundable fee of US$ 10000.

(c) Check whether the issuing company has obtained the necessary approvals or exemption from the appropriate authorities from the country of its incorporation under the relevant laws relating to issue of capital, where required.

(d) Check whether the issuing company has appointed an overseas custodian bank, a domestic depository and a merchant banker for the purpose of issue of IDRs.

(e) Check whether the issuing company has delivered the underlying equity shares or cause them to be delivered to an Overseas Custodian Bank and the said bank has authorized the domestic depository to issue IDRs.

(f) Check whether the issuing company has filed through a merchant banker or the domestic depository a due diligence report with the Registrar and with SEBI in the form specified.

(g) Check whether the draft prospectus has been filed with SEBI, through the merchant banker, at least 21 days prior to the filing a prospectus/letter of offer.

(h) Check whether the issuing company has through a merchant Banker filed a prospectus certificated by two authorized signatories of the issuing company, one of whom shall be a whole-time director and other the Chief Accounts Officer, stating the particulars of the resolution of the Board by which it was approved, with the SEBI and Registrar of Companies, New Delhi, before such issue.

(i) Whether the company has obtained in principle listing permission from one or more stock exchanges having nation wide trading terminals in India.

(j) Check whether the issuing company has appointed underwriters registered with SEBI to underwrite the issue of IDRs.

3. Limits

Check the IDRs issued in any financial year has not exceeded 25 per cent of its post issue number of equity shares of the company.

4. Registration of documents

(a) Check whether the Merchant banker to the issue of IDRs has delivered for registration the following documents or information to the SEBI and Registrar of Companies Act, New Delhi, namely:

   — instrument constituting or defining the constitution of the issuing company;
   — the enactments or provisions having the force of law by or under which the incorporation of the issuing company was effected, a copy of such provisions attested by an officer of the company be annexed;
   — if the issuing company has established place of business in India, address of its principal office in India;
— if the issuing company does not establish principal place of business in India, an address in India where the said instrument, enactments or provision or copies thereof are available for public inspection, and if these are not in English, a translation thereof certified by a responsible officer of the issuing company shall be kept for public inspection;
— a certified copy of the certificate of incorporation of the issuing company in the country in which it is incorporated;
— copies of the agreements entered into between the issuing company, the overseas custodian bank, the domestic depository, which shall inter alia specify the rights to be passed on to the IDR holders;
— if any document or any portion thereof required to be filed with the SEBI/ Registrar of Companies is not in English language, a translation of that document or portion thereof in English, certified by a responsible officer of the company to be correct and attested by an authorised officer of the Embassy or Consulate of that country in India, shall be attached to each copy of the document.
(b) Check whether the prospectus filed with the SEBI and Registrar is containing the particulars as prescribed in Schedule to these rules and has been signed by all the whole-time directors of the issuing company and by the Chief Accounts Officer.

5. Condition for issue of prospectus and application

(a) Check whether the application form is accompanied by a memorandum containing the salient features of prospectus in specified form. However, in case of invitation to enter into an underwriting agreement with respect to IDRs, such memorandum need not accompany the application.

(b) Check whether the prospectus for subscription of IDRs of the issuing company includes a statement purporting to be made by an expert? If so, check whether the expert has given his written consent to the issue thereof and has not withdrawn such consent before the delivery of a copy of the prospectus to the SEBI and Registrar of Companies, New Delhi, appears on the prospectus.

(c) Check whether the person(s) responsible for issue of the prospectus has not incurred any liability by reason of any non-compliance with or contravention of any provision of this rule, if—

(i) as regards any matter not disclosed he proves that he had no knowledge thereof; or

(ii) the contravention arose in respect of such matters which in the opinion of the Central Government were not material.

6. Listing of Indian Depository Receipt

IDRs issued has to be listed on the recognized Stock Exchange(s) in India having nationwide terminals.

7. Procedure for transfer and redemption

(a) Check whether the company has complied with FEMA and exchange control
requirements in respect of redemption of IDRs especially with respect to provisions relating to export of foreign exchange.

(b) Check whether the following procedure has been followed while redemption of IDRs.

1. The resident holder of IDR contact Domestic Depository to redeem IDRs subject to the provision of FEMA.

2. Domestic Depository request the Overseas Custodian Bank to get the corresponding underlying equity shares released in favour of Indian resident for being sold directly on behalf of Indian Resident or being transferred in the books of issuing company in the name of Indian Resident and

3. A copy of such request has to be sent to the issuing Company for information.

However, the IDRs issued by an issuing company may be purchased, possessed and transferred by a person other than a person resident in India if such Issuing Company obtains specific approval from Reserve Bank of India in this regard or complies with any policy or guidelines that may be issued by RBI on the subject matter.

8. Continuous Disclosure Requirements

(a) Check whether the issuing company has furnished to the Overseas Custodian Bank and Domestic Depository, a certificate obtained by it from the statutory auditor of the company or a Chartered Accountant about utilization of funds and its variation from the projections of utilization of funds made in the prospectus, if any, in quarterly intervals and shall also publish it or cause to be published in one of the English language newspapers having wide circulation in India.

(b) Check whether the quarterly audited financial results has been prepared and published in newspapers in the manner specified by the listing conditions.

9. Distribution of corporate benefits

Check whether, on the receipt of dividend or other corporate action on the IDRs as specified in the agreements between the issuing company and the Domestic Depository, the Domestic Depository has distributed them to the IDR holders in proportion to their holdings of IDRs.

10. Penalty

If a company or any other person contravenes any provision of these rules for which no punishment is provided in the Act, the company and every officer of the company who is in default or such other person shall be punishable with the fine which may extend to twice the amount of the IDR issue and where the contravention is a continuing one, with a further fine which may extend to five thousand rupees for every day, during which the contravention continues.
Check list under Chapter VIII SEBI (Issue of Capital and Disclosure Requirements) Regulations 2009 for issue of Indian Depository Receipts

Eligibility

Ensure that
(a) the issuing company is listed in its home country;
(b) the issuing company is not prohibited to issue securities by any regulatory body;
(c) the issuing company has track record of compliance with securities market regulations in its home country.

Explanation: For the purpose of this regulation, the term “home country” means the country where the issuing company is incorporated and listed.

Conditions for issue of IDR

Ensure that the following conditions are satisfied
(a) issue size shall not be less than fifty crore rupees;
(b) procedure to be followed by each class of applicant for applying shall be mentioned in the prospectus;
(c) minimum application amount shall be twenty thousand rupees;
(d) at least fifty per cent. of the IDR issued shall be allotted to qualified institutional buyers on proportionate basis as per illustration given in Part C of Schedule XI;
(e) the balance fifty per cent. may be allocated among the categories of noninstitutional investors and retail individual investors including employees at the discretion of the issuer and the manner of allocation shall be disclosed in the prospectus. Allotment to investors within a category shall be on proportionate basis:
It may be noted that at least thirty per cent. of the said fifty per cent. IDR issued shall be allocated to retail individual investors and in case of under-subscription in retail individual investor category, spill over to the extent of under-subscription shall be permitted to other categories.
(f) At any given time, there shall be only one denomination of IDR of the issuing company.

Minimum subscription

For non-underwritten issues
(a) If the issuing company does not receive the minimum subscription of ninety per cent of the offer through offer document on the date of closure of the issue, or if the subscription level falls below ninety per cent. after the closure of issue on account of cheques having been returned unpaid or withdrawal of applications, the issuing company shall forthwith refund the entire subscription amount received.
(b) If the issuing company fails to refund the entire subscription amount within fifteen days from the date of the closure of the issue, it is liable to pay the amount with interest to the subscribers at the rate of fifteen per cent. per annum for the period of delay.

For underwritten issues
If the issuing company does not receive the minimum subscription of ninety per cent. of the offer through offer document including devolvement of underwriters within sixty days from the date of closure of the issue, the issuing company shall forthwith refund the entire subscription amount received with interest to the subscribers at the rate of fifteen per cent. per annum for the period of delay beyond sixty days.

Fungibility

3 As per the supplement to Study Material
The Indian depository Receipts shall not be automatically fungible into underlying equity shares of issuing company.

**Filing of draft prospectus, due diligence certificates, payment of fees and issue advertisement for IDR**

The issuing company making an issue of IDR shall enter into an agreement with a merchant banker on the lines of format of agreement specified.

If the issue is managed by more than one merchant banker, the rights, obligations and responsibilities, relating inter-alia to disclosures, allotment, refund and underwriting obligations, if any, of each merchant banker shall be predetermined and disclosed in the prospectus on the lines of format as specified in the Schedule.

The issuing company shall file a draft prospectus with the Board through a merchant banker along with the requisite fee, as prescribed in Companies (Issue of Indian Depository Receipts) Rules, 2004.

The prospectus filed with the Board under this regulation shall also be furnished to the Board in a soft copy on the lines specified in the Schedule.

(5) The lead merchant bankers shall:

(a) Submit a due diligence certificate as per specified format to the Board along with the draft prospectus.

(b) Certify that all amendments, suggestions or observations made by the Board have been incorporated in the prospectus.

(c) Submit a fresh due diligence certificate as per format specified, at the time of filing the prospectus with the Registrar of the Companies.

(d) Furnish a certificate as per specified format, immediately before the opening of the issue, certifying that no corrective action is required on its part.

(e) Furnish a certificate as per specified format, after the issue has opened but before it closes for subscription.

(6) The issuing company shall make arrangements for specified mandatory collection centres.

(7) The issuing company shall issue an advertisement in one English national daily newspaper with wide circulation and one Hindi national daily newspaper with wide circulation, soon after receiving final observations, if any, on the publicly filed draft prospectus with the Board, which shall be on the lines of the format and contain the minimum disclosures as required.

**Display of bid data**

The stock exchanges offering online bidding system for the book building process shall display on their website, the data pertaining to book built IDR issue, in the format specified, from the date of opening of the bids till at least three days after closure of bids.

**Disclosures in prospectus and abridged prospectus**

The prospectus shall contain all material disclosures which are true, correct and adequate so as to enable the applicants to take an informed investment decision.

The prospectus shall contain:

(a) the disclosures specified in Schedule to Companies (Issue of Indian Depository Receipts) Rules, 2004; and

(b) the specified disclosures.

(3) The abridged prospectus for issue of Indian Depository Receipts shall contain the specified disclosures.

**Post-issue reports**

The merchant banker shall submit post-issue reports to the Board as follows:
(a) initial post issue report, within three days of closure of the issue;
(b) final post issue report, within fifteen days of the date of finalisation of basis of allotment or within fifteen days of refund of money in case of failure of issue.

**Undersubscribed issue**
In case of undersubscribed issue of IDR, the merchant banker shall furnish information in respect of underwriters who have failed to meet their underwriting devolvement to the Board on the lines of the format specified.

**Finalisation of basis of allotment**
The executive director or managing director of the stock exchange, where the IDR are proposed to be listed, along with the post issue lead merchant bankers and registrars to the issues shall ensure that the basis of allotment is finalised in a fair and proper manner in accordance with the specified allotment procedure.

(c) **Listing Agreement for Indian Depository Receipts (IDRs)**

1. **Board Meeting**
   - Check whether the Company has notified stock exchange at least 7 days in advance of the date of the meeting of its Board of Directors at which the recommendation or declaration of a dividend or a rights issue or convertible debentures or of debentures carrying a right to subscribe to equity shares or the passing over of the dividend were considered.
   - Check whether the Company has within 15 minutes of Board Meeting, intimated to the Stock Exchange, by phone, fax, telegram, e-mail, the details on all dividends and/or cash bonuses recommended or declared or the decision to pass any dividend or interest payment, short particulars of any increase of capital whether by issue of bonus shares through capitalization, or by issue of rights shares, or in any other manner; short particulars of the reissues of forfeited shares or securities, or the issue of shares or securities held in reserve for future issue or the creation in any form or manner of new shares or securities or any other rights, privileges or benefits to subscribe thereto; short particulars of any other alterations of capital, including calls; or any other information necessary to enable the holders of the IDRs to appraise the issuer’s position and to avoid the establishment of a false market.

2. **Intimation/filing/submissions to stock exchange/s**
   - Check whether the Company has notified the stock exchange at least twenty-one days in advance of the date on and from which the dividend on shares will be payable.
   - Check whether the Company has submitted to the exchange documents such as Copy of SEBI observation letter on draft prospectus, due diligence report from depository, merchant bankers certificate reporting positive compliance.
   - Check whether the issuer, in case of granting any options, has notified Stock Exchange number of shares covered by such options, of the terms thereof and of the time within which they may be exercised and any subsequent changes or cancellation or exercise of such options.
   - Check whether the company has notified any change in the rights attaching to any class of equity shares into which the IDRs are exchangeable.
— Check whether the company has notified change in the constitution of Board, Managing Director, Auditor, Compliance officer, domestic depository, overseas custodian etc

— Check whether the Company has forwarded to stock exchange promptly the following:
  — copies of the Annual Reports, which shall include the Balance Sheet and Profit & Loss Account, Directors’ Report and the Auditors’ Report and of all periodical and special reports as soon as they are issued;
  — copies of all notices, resolutions and circulars relating to new issue of capital prior to their dispatch to the equity shareholders or IDR holders;
  — copies of all the notices, call letters or any other circulars including notices of meetings at the same time as they are sent to the equity shareholders, IDR holders, debenture holders or creditors or any class of them or as they are advertised in the Press.
  — copy of the proceedings at all Annual and Extraordinary General Meetings of the Issuer;
  — copy of the deposit agreement as soon as it is executed.
  — copies of all notices, circulars, etc., issued or advertised in the press either by the Issuer, or by any other body corporate which the Issuer proposes to absorb or with which the Issuer proposes to merge or amalgamate, or under orders of the court or any other statutory authority in connection with any merger, amalgamation, re-construction, reduction of capital, scheme or arrangement, including notices, circulars, etc. issued or advertised in the press in regard to meetings of equity shareholders, IDR holders or any class of them and copies of the proceedings at all such meetings.

— Check whether the company has filed with the Exchange the shareholding pattern on a quarterly basis within 15 days of end of the quarter in the prescribed form

— Check Issuer has intimated to the Stock Exchanges, immediately of events such as strikes, lock outs, closure on account of power cuts, etc. and all events which will have a bearing on the performance/operations of the company as well as price sensitive information both at the time of occurrence of the event and subsequently after the cessation of the event.

— Check whether the company has informed stock exchange about material events such as Change in the general character or nature of business, Disruption of operations due to natural calamity, Commencement of Commercial Production/Commercial Operations, Developments with respect to pricing/realisation arising out of change in the regulatory framework, Litigation/dispute with a material impact, Revision in Ratings etc

— Check whether the company has furnished on a quarterly basis a statement to the stock exchange indicating the variations between projected utilisation of funds and/or projected profitability statement made by it in its prospectus or letter of offer and the actual utilisation of funds and/or actual profitability.
— Check whether the company has furnished a copy of agreement or MOU entered into with overseas custodian bank, domestic depository, merchant banker and RTA to the stock exchange.

3. Issuance of further IDRs

— Check whether the company has obtained ‘in-principle’ approval and made application for listing, in respect of further issue of IDRs if any,

— Check whether the Company has complied with all legal and regulatory requirements before issuing any prospectus/offer document/letter of offer for public subscription of any IDRs.

— Check whether the company has made the allotment of IDRs offered to the public within 30 days of the closure of the public issue and has paid interest @ 15% per annum if the allotment has not been made and or refund orders have not been dispatched to the investors within 30 days from the date of the closure of the issue.

— Check whether the underlying shares of IDRs ranks pari passu with the existing shares of the same class and the fact of having different classes of shares based on different criteria, if any, has been disclosed by the company in every offer document issued in India and in the annual report.

4. Corporate Governance

Composition of Board

— Check whether the Board of the company has optimum combination of executive/non-executive director and with prescribed minimum Percentage of Independent Directors

— Check whether all fees/compensation, if any paid to non-executive directors, including independent directors, has been fixed by the Board of Directors and with previous approval of shareholders in general meeting.

— Check whether the Board has met at least four times a year, with a maximum time gap of four months between any two meetings.

— Check whether no director is a member in more than 10 committees or act as Chairman of more than five committees across all companies in which he is a director.

— Check whether the Board periodically reviews compliance reports of all laws applicable to the company, prepared by the company as well as steps taken by the company to rectify instances of non-compliances.

— Check whether the Board has laid down a code of conduct for all Board members and senior management of the company and the same is posted on the website of the company.

— Check whether all Board members and senior management personnel affirms compliance with the code on an annual basis.

— Check whether the Annual Report of the company contains a declaration to this effect signed by the CEO.
Audit Committee

— Check whether a qualified and independent Audit Committee has been set up, with minimum three directors as members and Two-thirds of them being independent.

— Check whether all members of Audit Committee are financially literate and at least one member has accounting or related financial management expertise.

— Check whether the Chairman of the Audit Committee is an independent director and was present at Annual General Meeting to answer shareholder queries.

— Check whether the Audit Committee has met at least four times in a year and not more than four months elapsed between two meetings.

— Check whether the Audit Committee has reviewed the following information:
  1. Management discussion and analysis of financial condition and results of operations;
  2. Statement of significant related party transactions (as defined by the Audit Committee), submitted by management;
  3. Management letters/letters of internal control weaknesses issued by the statutory auditors;
  4. Internal audit reports relating to internal control weaknesses; and
  5. The appointment, removal and terms of remuneration of the Chief Internal Auditor shall be subject to review by the Audit Committee.

Subsidiary Companies

— Check whether at least one independent director on the Board of Directors of the holding company is a director on the Board of Directors of a material non-listed Indian subsidiary company.

— Check whether the Audit Committee of the listed holding company review the financial statements, in particular, the investments made by the unlisted subsidiary company.

— Check whether the minutes of the Board meetings of the unlisted subsidiary company was placed at the Board meeting of the listed holding company.

Disclosures

— Check whether the company has disclosed related party transactions if any to the audit committee.

— Check whether the company has disclosed to the Audit Committee about accounting treatment which is different from prescribed accounting standard.

— Check whether the company has laid down procedures to inform Board members about the risk assessment and minimization procedures.

— Check whether the company has disclosed to the Audit Committee the uses and applications of funds arising out of an IPO.
Remuneration of Directors

— Check whether all pecuniary relationship or transactions of the non-executive directors vis-à-vis the company has been disclosed in the Annual Report.

— Check whether the following disclosures on the remuneration of directors has been made in the section on the corporate governance of the Annual Report:

(a) All elements of remuneration package of individual directors summarized under major groups, such as salary, benefits, bonuses, stock options, pension etc.

(b) Details of fixed component and performance linked incentives, along with the performance criteria.

(c) Service contracts, notice period, severance fees.

(d) Stock option details, if any - and whether issued at a discount as well as the period over which accrued and over which exercisable.

— Check whether the company has published its criteria of making payments to non-executive directors in its annual report. Alternatively, this may be put up on the company's website and reference drawn thereto in the annual report.

— Check whether the company has disclosed the number of shares and convertible instruments held by non-executive directors in the annual report.

Management

— Check whether, as part of the directors' report or as an addition thereto, a Management Discussion and Analysis report is forming part of the Annual Report to the shareholders with specified information.

— Check whether Senior management has made disclosures to the board relating to all material financial and commercial transactions, where they have personal interest, that may have a potential conflict with the interest of the company at large (for e.g. dealing in company shares, commercial dealings with bodies, which have shareholding of management and their relatives etc.).

Shareholders

— Check, in case of the appointment of a new director or re-appointment of a director the shareholders has been provided with the following information:

— A brief resume of the director;

— Nature of his expertise in specific functional areas;

— Names of companies in which the person also holds the directorship and the membership of Committees of the Board; and

— Shareholding of non-executive directors as stated in clause 24 (IV)(E)(v) above.

— Check whether Quarterly results and presentations made by the company to analysts has been put on company’s website, or shall be sent in such a form so as to enable the stock exchange on which the company is listed to put it on its own website.
Check whether a board committee under the chairmanship of a non-executive director has been formed to specifically look into the redressal of shareholder and investors complaints like transfer of shares, non-receipt of balance sheet, non-receipt of declared dividends etc.

**CEO/CFO certification**

Check whether the CEO, i.e. the Managing Director or Manager appointed in terms of the Companies Act, 1956 and the CFO i.e. the whole-time Finance Director or any other person heading the finance function discharging that function has certified to the Board that:

(a) They have reviewed financial statements and the cash flow statement for the year and that to the best of their knowledge and belief:

   (i) these statements do not contain any materially untrue statement or omit any material fact or contain statements that might be misleading;

   (ii) these statements together present a true and fair view of the company’s affairs and are in compliance with existing accounting standards, applicable laws and regulations.

(b) There are, to the best of their knowledge and belief, no transactions entered into by the company during the year which are fraudulent, illegal or violative of the company’s code of conduct.

(c) They accept responsibility for establishing and maintaining internal controls for financial reporting and that they have evaluated the effectiveness of internal control systems of the company pertaining to financial reporting and they have disclosed to the auditors and the Audit Committee, deficiencies in the design or operation of such internal controls, if any, of which they are aware and the steps they have taken or propose to take to rectify these deficiencies.

(d) They have indicated to the auditors and the Audit Committee

   (i) significant changes in internal control over financial reporting during the year;

   (ii) significant changes in accounting policies during the year and that the same have been disclosed in the notes to the financial statements; and

   (iii) instances of significant fraud of which they have become aware and the involvement therein, if any, of the management or an employee having a significant role in the company’s internal control system over financial reporting.

**Report on Corporate Governance**

Check whether there is a separate section on Corporate Governance in the Annual Reports of company, with a detailed compliance report on Corporate Governance.

Check whether the company has submitted a quarterly compliance report to the stock exchanges within 15 days from the close of quarter as per the specified format.
Compliance

Check whether the company has obtained a certificate from either the auditors or practising company secretaries regarding compliance of conditions of corporate governance as stipulated in this clause and annex the certificate with the directors’ report, which is sent annually to all the shareholders of the company and has been sent to the Stock Exchanges along with the annual report filed by the company.

5. EDIFAR System

Check whether the company has filed necessary documents in the EDIFAR system.

6. Actions/investigations initiated

Check whether the issuer has intimated any action/investigations initiated by any statutory/regulatory authority along with the purpose of the same.

7. Information/submissions to IDR holders

Check whether the issuer has sent a copy of Annual Report containing Boards Report, Profit & Loss Account, Balance Sheet, Cash flow statement, Auditors report etc within four months of the end of financial year.

Check whether the company has disclosed the pre and post arrangement capital structure and shareholding pattern to the IDR holders in case of corporate restructuring like mergers/amalgamations and other schemes in advance.

8. Annual Report/publications etc

— Check whether the Issuer has sent to its IDR holders and the stock exchange a copy of the annual report within four months of the end of the financial year. The annual report shall contain the Board’s report, Balance Sheet, Profit and Loss Account, Cash Flow Statement and the auditor’s report thereon.

— Check whether the company has complied either with Indian GAAP (including all Accounting Standards issued by the Institute of Chartered Accountants of India) or with the International Financial Reporting Standards (IFRS) [including the International Accounting Standards (IAS)] or with US GAAP in the preparation and disclosure of its financial results.

— In case the Company opts to prepare and disclose its financial results as per IFRS/US GAAP, Check whether it has complied with the requirements of clauses 35 and 36 of listing agreement for IDR.

— In case the Company opts to prepare and disclose its financial results as per Indian GAAP, Check whether the company has complied with , as far as may be, with clauses 37 and 38 of the listing agreement for IDR and with the provisions of the Companies Act, 1956 relating to authentication and presentation of annual accounts as far as may be practicable.

9. Audit Qualifications

Check whether there are any qualifications in the Audit report? If so check
whether it is published along with audited financial statements.

10. Appointment of Company Secretary

Check whether the company has appointed the Company Secretary as Compliance Officer who will directly liaise with the authorities such as SEBI, Stock Exchanges, ROC etc., and investors with respect to implementation of various clause, rules, regulations and other directives of such authorities and investor service & complaints related matter.

11. Undertaking of Due diligence

Check whether the company has undertaken a due diligence survey to ascertain whether the RTA is sufficiently equipped with infrastructure facilities such as adequate manpower, computer hardware and software, office space, documents handling facility etc., to serve the IDR holders.

12. Equivalent Information

Check whether the Company has provided any information simultaneously, that was furnished to international exchanges.

13. Miscellaneous

Check whether any scheme of arrangement/amalgamation/merger/reconstruction/reduction of capital, etc., presented by the Company to any Court or Tribunal has not violated in any way violate, override or circumscribe the provisions of securities laws or the stock exchange requirements.

Check whether the issuer has complied with the rules/regulations/laws of the country of origin.

IV. PENAL PROVISIONS RELATING TO IDRs UNDER VARIOUS LEGISLATIONS

(a) Companies Act, 1956

Section 606, 607 and 608 of the Act prescribe the penalty for non-compliance of any of the provisions relating to IDR which is reproduced below:

606. Penalty for contravention of Sections 603, 604, 605 and 605A

Any person who is knowingly responsible—

(a) for the issue, circulation or distribution of a prospectus; or

(b) for the issue of a form of application for shares, debentures or Indian Depository Receipts;

in contravention of any of the provisions of Sections 603, 604, 405 and 605A, shall be punishable with imprisonment for a term which may extend to six months, or with fine which may extend to fifty thousand rupees, or with both.

607. Civil liability for misstatements in prospectus
Section 62 shall extend to every prospectus offering for subscription shares in or debentures of a company incorporated or to be incorporated outside India, whether the company has or has not established, or when formed will or will not establish, a place of business in India, with the substitution for references in Section 62 to Section 60 of this Act, of references to Section 604 thereof.

608. Interpretation of provisions as to prospectus

(1) Where any document by which any shares in, or debentures of, a company incorporated outside India are offered for sale to the public, would, if the company concerned had been a company within the meaning of this Act, have been deemed by virtue of Section 64, to be a prospectus issued by the company, that document shall be deemed, for the purposes of this Part, to be a prospectus issued by the company offering such shares or debentures for subscription.

(2) An offer of shares or debentures for subscription or sale to any person whose ordinary business it is to buy or sell shares or debentures, whether as principal or as agent, shall not be deemed to be an offer to the public for the purposes of this Part.

(3) In this Part, the expressions “prospectus”, “shares” and “debentures” have the same meanings as when used in relation to a company incorporated under this Act.

(b) Companies (Issue of Indian Depository Receipts) Rules, 2004 (Rule 13)

As per the Rules, if a company or any other person contravenes any provision of these rules for which no punishment is provided in the Act, the company and every officer of the company who is in default or such other person shall be punishable with the fine which may extend to twice the amount of the IDR issue and where the contravention is a continuing one, with a further fine which may extend to five thousand rupees for every day, during which the contravention continues.

As per Rule 8(iv), the person(s) responsible for issue of the prospectus shall not incur any liability by reason of any non-compliance with or contravention of any provision of this rule, if—

(a) as regards any matter not disclosed, he proves that he had no knowledge thereof; or

(b) the contravention arose in respect of such matters which in the opinion of the Central Government were not material.

(c) Securities Contracts Regulation Act, 1956

Apart from the above, non-compliance of the conditions of the listing agreement attracts the provisions of Section 23(2) and 23E of the SCRA which is given hereunder:

— 23(2) – imprisonment of 10 years or fine of Rs. 25 crores or both for non-compliance of conditions of listing.

— 23E of SCRA, 1956 – failure to comply with conditions of listing or delisting or committing a breach thereof – Rs. 25 crores fine.
(d) **Foreign Exchange Management Act, 1999**

Non-compliance of FEMA provisions attracts the following:

1. If any person contravenes any provision of this Act, or contravenes any rule, regulation, notification, direction or order issued in exercise of the powers under this Act, or contravenes any condition subject to which an authorization is issued by the Reserve Bank, he shall, upon adjudication, be liable to a penalty up to thrice the sum involved in such contravention where such amount is quantifiable, or up to two lakh rupees where the amount is not quantifiable, and where such contravention is a continuing one, further penalty which may extend to five thousand rupees for every day after the first day during which the contravention continues.

2. Any Adjudicating Authority adjudging any contravention under sub-section (1), may, if he thinks fit in addition to any penalty which he may impose for such contravention direct that any currency, security or any other money or property in respect of which the contravention has taken place shall be confiscated to the Central Government and further direct that the foreign exchange holdings, if any of the persons committing the contraventions or any part thereof, shall be brought back into India or shall be retained outside India in accordance with the directions made in this behalf.

*Explanation*: For the purposes of this sub-section, “property” in respect of which contravention has taken place, shall include:

(a) deposits in a bank, where the said property is converted into such deposits;

(b) Indian currency, where the said property is converted into that currency; and

(c) any other property which has resulted out of the conversion of that property.

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**ANNEXURE A**

**LISTING AGREEMENT FOR IDRs - HIGHLIGHTS**

<table>
<thead>
<tr>
<th>Reference</th>
<th>Subject matter</th>
<th>Requirement</th>
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</thead>
<tbody>
<tr>
<td>Clause 1</td>
<td>Share allotment; advices of rights entitlement</td>
<td>Allotment should be made simultaneously and that in the event of its being impossible to issue letters of regret at the same time, a notice to that effect will be inserted in the press so that it will appear on the morning after the letters of allotment have been posted; advices of rights entitlement, wherever applicable, should be issued simultaneously.</td>
</tr>
<tr>
<td>Clause 2</td>
<td>Intimation of date of Board Meeting</td>
<td>The Issuer is required to notify stock exchange at least 7 days in advance of the date of the meeting of its Board of Directors at which the recommendation or declaration of a dividend or a rights issue or convertible debentures, proposal for declaration of any</td>
</tr>
<tr>
<td>Clause 3</td>
<td>Intimation after Board Meeting</td>
<td>The Issuer is required to, immediately after the meeting of its Board of Directors has been held to consider or decide the same, intimate to the Stock Exchange, (within 15 minutes of the closure of the board meeting) by phone, fax, telegram, e-mail about decision on recommendation/declaration of dividend, matters such as the total turnover, gross profit/loss, provision for depreciation, tax provisions and net profits for the year etc.,</td>
</tr>
<tr>
<td>Clause 4</td>
<td>Intimation to stock exchange on dividend payment</td>
<td>The Issuer is required to notify the stock exchange at least twenty-one days in advance of the date on and from which the dividend on shares will be payable.</td>
</tr>
<tr>
<td>Clause 6</td>
<td>Intimation to Stock Exchange about increase of capital, re-issue of forfeited shares etc.,</td>
<td>The Issuer is required to within 15 minutes of the closure of any board meeting intimate to the Stock Exchanges by phone, fax, telegram, e-mail about short particulars of any increase of capital, short particulars of the reissues of forfeited shares or securities, or the issue of shares or securities held in reserve for future issue or the creation in any form or manner of new shares or securities or any other rights, privileges or benefits to subscribe thereto, short particulars of any other alterations of capital, including calls, any other information necessary to enable the holders of the IDRs to appraise the issuer’s position and to avoid the establishment of a false market.</td>
</tr>
<tr>
<td>Clause 8</td>
<td>In-principal Approval/filing of certain documents with stock exchange on further issues</td>
<td>The issuer is required to obtain ‘in-principle’ approval for listing from the exchanges where its IDRs are listed, before issuing further IDRs. The issuer is required to submit documents such as copy of SEBI’s observation letter on prospectus, due diligence report from domestic depository etc.</td>
</tr>
<tr>
<td>Clause 11</td>
<td>Intimation to Stock exchange on matters pertaining to constitution of Board, Auditor, Compliance</td>
<td>The issuer is required to notify promptly to the stock exchange about change in the constitution of Board, Managing Director, Compliance officer, Auditor, Domestic Depository etc.,</td>
</tr>
<tr>
<td>Clause 12</td>
<td>Forwarding copies of notices, annual reports etc to stock exchange</td>
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<tr>
<td></td>
<td>Copies of all notices, resolutions and circulars relating to new issue of capital prior to their dispatch to the equity shareholders or IDR holders; copies of all the notices, call letters or any other circulars including notices of meetings at the same time as they are sent to the equity shareholders, IDR holders, debenture holders or creditors or any class of them or as they are advertised in the Press; copy of the proceedings at all Annual and Extraordinary General Meetings of the Issuer; copy of the deposit agreement as soon as it is executed; copies of all notices, circulars, etc., issued or advertised in the press etc.,</td>
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<tr>
<td>Clause 14</td>
<td>Filing of shareholding pattern</td>
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<td></td>
<td>The issuer is required to file with the Exchange the shareholding pattern on a quarterly basis within 15 days of end of the quarter in the prescribed form.</td>
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<tr>
<td>Clause 15</td>
<td>The Issuer is required to intimate to the Stock Exchanges, immediately of events such as strikes, lock outs, closure on account of power cuts, etc. and all events which will have a bearing on the performance/operations of the company as well as price sensitive information.</td>
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<tr>
<td>Clause 20</td>
<td>Intimation on Variation on projected and actual profitability statement</td>
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<td>The Issuer is required furnish on a quarterly basis a statement to the stock exchange indicating the variations between projected utilisation of funds and/or projected profitability statement made by it in its prospectus or letter of offer and the actual utilisation of funds and/or actual profitability.</td>
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<tr>
<td>Clause 23</td>
<td>Appointment of Company Secretary, undertaking of due diligence etc.</td>
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|           | The Issuer is required to:  
(a) appoint the Company Secretary of the Issuer as Compliance Officer who will directly liaise with the authorities such as SEBI, Stock Ex-changes, ROC etc., and investors with respect to implementation of various clause, rules, regulations and other directives of such authorities and investor service & complaints related matter.  
(b) undertake a due diligence survey to |
ascertain whether the RTA is sufficiently equipped with infrastructure facilities such as adequate manpower, computer hardware and software, office space, documents handling facility etc., to serve the IDR holders.

(c) furnish a copy of agreement or MOU entered into with overseas custodian bank, domestic depository, merchant banker and RTA to the stock exchange

<table>
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<th>Clause 24</th>
<th>Corporate Governance</th>
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<td>(a) Composition of the Board</td>
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<td>(b) Non-executive directors’ compensation and disclosures</td>
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<td>(c) Other provisions as to Board and Committees</td>
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<td>(d) Code of Conduct for the Board</td>
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<td>(e) Audit Committee, its meeting powers, role</td>
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<td>(f) Subsidiary companies</td>
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<td>(i) Report on Corporate Governance</td>
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<tr>
<td></td>
<td></td>
<td>(j) Compliance Certificate from Practising Company Secretary or auditors</td>
</tr>
</tbody>
</table>

| Clause 34-38 | Disclosure & publication of financial results | Disclosure depends on whether issuer opts to comply with Indian GAAP/US GAAP/International Financial Reporting Standard (IFRS) |

| Clause 39 | Equivalent information | Information furnished to any international stock exchanges has to be furnished to Indian Stock Exchanges where IDRs are listed. |

**Listing agreement for IDR issuers having its registered office situated in a country, the securities market regulator of which is a signatory to MMOU of IOSCO**

In order to reduce the additional regulatory or cost burden to the issuers, it has been decided by SEBI to simplify the listing requirements applicable to the issuers from the countries which are the signatories of Multilateral Memorandum of Understanding (MMOU) of International Organization of Securities Commissions (IOSCO). Accordingly, SEBI has drafted a model listing agreement for IDR issuers having its registered office situated in a country, the securities market regulator of
which is a signatory to MMOU of IOSCO. With respect to most of the provisions especially Corporate Governance requirements and disclosure of periodical results, the issuer is allowed to follow the home country requirements provided equitable treatment is given to the IDR holders vis-à-vis holders of equity shares. For the issuing companies from other jurisdictions, the existing model listing agreement for IDRs shall continue to apply till further advice in this regard.

**Highlights**

1. The Company should for all corporate actions (except those which are not permitted by Indian laws), will treat holders of IDRs (hereinafter referred to as “IDR Holders”), in a manner equitable with the holders of its equity shares in the home country;

2. The issuing company is required to notify the stock exchange at the same time it intimates to any other exchange, where its equity shares are listed, regarding the meeting, at which matters such as the recommendation or declaration of dividend or rights issue or issue of convertible debentures or of debentures carrying a right to subscribe to equity shares or the passing over of the dividend and any decision on buy back of equity shares of the issuing company, are due to be considered.

3. The issuing company is required to intimate to the stock exchange after the meeting of its Board of Directors has been held to consider or decide the following, at the same time and to the extent it intimates the same to the listing authority in its home country or other jurisdictions where its securities may be listed, by electronic filing:

   (a) all dividends and/or cash bonuses recommended or declared or the decision to pass any dividend or cash bonus; and

   (b) the total turnover, gross profit/loss, provision for depreciation, tax provisions and net profits for the year (with comparison with the previous year) and the amounts appropriated from reserves, capital profits, accumulated profits of past years or other special source to provide wholly or partly for any dividend, even if this calls for qualification that such information is provisional or subject to audit.

4. The issuing company is required to notify the stock exchange at least seven working days in advance of the record date for the corporate actions like rights, bonus, splits and payment of any dividend to IDR Holders. The issuing company further agrees that the process for setting a record date for any corporate action will be disclosed in the offer document and prior intimation will be provided to the stock exchange and in the media if this process changes.

5. The issuing company is required to pay the dividend as per the timeframe applicable in its home country or other jurisdictions where its securities are listed, whichever is earlier, so as to reach the IDR Holders on or before the date fixed for payment of dividend to holders of its equity share or other securities.
6. The issuing company is required to promptly disclose to the stock exchanges the following by electronic filing:

(a) short particulars of any increase of capital whether by issue of bonus shares through capitalization, or by rights issue of equity shares, or in any other manner;

(b) short particulars of the reissues of forfeited shares or securities, or the issue of shares or securities held in reserve for future issue or the creation in any form or manner of new shares or securities or any other rights, privileges or benefits to subscribe thereto;

(c) short particulars of any other alterations of capital, including calls; and

(d) any other information necessary to enable the IDR Holders to appraise the issuing company's position and to avoid the establishment of a false market in IDRs;

7. The issuing company is required to declare that the underlying equity shares, against which the IDRs are issued, have been/will be listed in its home country before the listing of IDRs in the stock exchange;

8. The issuing company is required to obtain 'in-principle' approval for listing from the stock exchanges where its IDRs are listed, before issuing further IDRs and to make an application to the stock exchange for the listing such further IDRs;

9. The issuing company agrees that it will promptly notify the stock exchange at the same time where it notifies to comply with listing requirements of home country or other jurisdictions where its securities may be listed any change in the Board, Auditors etc.

10. The company is to required to forward the Annual Report/notices etc at the same time and as to the extent that it discloses to holders of securities in its home country or in other jurisdictions where such securities are listed.

11. The issuing company agrees to file with the stock exchange the pattern of IDR Holders on a quarterly basis within 15 days of end of the quarter in the prescribed form.

12. The issuing company is required to comply with the Corporate Governance provisions as applicable in its home country and other jurisdictions in which its equity shares are listed. Further the issuing company hereby agrees to file a comparative analysis of the corporate governance provisions that are applicable in its home country and in the other jurisdictions in which its equity shares are listed along with the compliance of the same vis-à-vis the corporate governance provisions applicable to Indian listed companies. The said report shall be filed at the time of filing the annual reports with stock exchange.

13. The Company is required to comply with Indian GAAP or International Financial Reporting Standards (IFRS) or US GAAP in the preparation and
disclosure of its financial results.

LESSON ROUND-UP

- Indian Depository Receipt means any instrument in the form of a depository receipt created by Domestic Depository in India against the underlying equity shares of issuing company.
- Domestic Depository is custodian of securities registered with SEBI and authorised by the issuing company to issue Indian Depository Receipts.
- Overseas Custodian Bank means a banking company which is established in a country outside India and has a place of business in India and acts as custodian for the equity shares of issuing company against which IDRs are proposed to be issued after having obtained permission from Ministry of Finance for doing such business in India.
- Issue of IDRs are regulated by Chapter VI A of SEBI (DIP) Guidelines, 2000 Companies (Issue of Indian Depository Receipts) Rules, 2004 and Listing Agreement for IDRs.
- The IDRs issued should be listed on the recognized Stock Exchange(s) in India as specified and such IDRs may be purchased, possessed and freely transferred by a person resident in India.
- Issuer of an IDR has to comply with the listing conditions stated in the listing agreement for IDRs.

SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

2. What are the procedures for making an issue of Indian Depository Receipts?
3. Explain the procedure for carrying out due diligence of IDR issue.
LEARNING OBJECTIVES
The objective of this study lesson is to enable the students to understand
- Concept and types of foreign investments in India
- Various entry options available for foreign investment
- Foreign Direct Investment Policy
- Procedure for setting up of joint venture
- Checklist in respect of setting up joint ventures

I. FOREIGN INVESTMENTS IN INDIA

Introduction
A series of ambitious economic reforms aimed at deregulating the economy and stimulating foreign investment has moved India firmly into the front runners of the rapidly growing Asia Pacific Region and unleashed the latent strength of a complex and rapidly changing nation. Today India is one of the most exciting emerging markets in the world. Skilled managerial and technical manpower that matches the best available in the world and a middle class whose size exceeds the population of the USA or the European Union, provide India with a distinct cutting edge in global competition. India’s time tested institutions offer foreign investors a transparent environment that guarantees the security of their long term investments. These include a free and vibrant press, a well established judiciary, a sophisticated legal and accounting system and a user friendly intellectual infrastructure. India’s dynamic and highly competitive private sector has long been the backbone of its economic activity and offers considerable scope for foreign direct investment, joint ventures and collaborations.

Before setting up a business entity, the foreign investor has to consider the factors such as the eligibility, fund raising avenues, special concessions, tax implications, different options in terms of form of business such as company, branch office etc, incentives and exemptions available, industry specific requirement, specific area requirements (State laws) etc.

The flow chart (on next page) describes the different forms of foreign Investment.

Statutory Basis
Foreign investment in India is governed by Foreign Direct Investment Policy and sub-section (3) of section 6 of the Foreign Exchange Management Act, 1999 read with Notification No. FEMA 20/2000-RB dated May 3, 2000, containing Foreign Exchange Management (Transfer or issue of security by a person resident outside India) Regulations, 2000 which has been amended from time to time. The FEMA regulation contains the procedural aspects pertaining to the mode of investments i.e. manner of receipt of funds, reporting of receipt of funds, reporting of issue of shares etc.

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Foreign Investments in India—schematic representation*

Entry Options

A foreign company planning to set up business operations in India has the following entry options:

Prohibited sectors for Foreign Investment

Foreign investment in India is freely permitted in almost all sectors except for the following prohibited sectors.

(i) Business of chit fund, or
(ii) Nidhi Company, or
(iii) Agricultural or plantation activities, or
(iv) Real estate business, or construction of farm houses
(v) Trading in Transferable Development Rights

Real Estate Business does not include development of townships, construction of residential/commercial premises, roads or bridges.

Further, Partnership firms/ proprietorship concerns having investments as per FEMA regulations are not allowed to engage in Print Media sector.

In addition to the above, investment in the form of Foreign Direct Investment is also prohibited in certain sectors such as:

(i) Retail Trading (except for single brand product retailing)
(ii) Atomic Energy
(iii) Lottery Business
(iv) Gambling and Betting
(v) Agriculture (excluding Floriculture, Horticulture, Development of seeds, Animal Husbandry, Pisciculture and Cultivation of vegetables, mushrooms etc. under controlled conditions and services related to agro and allied sectors) and Plantations (Other than Tea plantations).

**Foreign Direct and Indirect Investment**

Investment in Indian companies can be made both by non-resident as well as resident Indian entities. Any non-resident investment in an Indian company is direct foreign investment. Investment by resident Indian entities could again comprise of both resident and non-resident investment. Thus, such an Indian company would have indirect foreign investment if the Indian investing company has foreign investment in it. The indirect investment can be a cascading investment i.e. through multi-layered structure also.

Recognising the need to bring in clarity, uniformity, consistency and homogeneity into the exact methodology of calculation across sectors/activities for all direct and indirect foreign investment in Indian companies, Government of India issue the guidelines for calculation of direct and indirect foreign investment.

Foreign Investment in Indian company shall include all types of foreign investments i.e. FDI, investment by FIIs, NRIs, ADRs, GDRs, Foreign Currency Convertible Bonds (FCCB) and convertible preference shares, convertible Currency Debentures etc.

All investment directly by a non-resident entity into the Indian company would be counted towards foreign investment.

The foreign investment through the investing Indian company would not be considered for calculation of the indirect foreign investment in case of Indian companies which are ‘owned and controlled’ by resident Indian citizens and/or Indian Companies which are owned and controlled by resident Indian citizens.
For this purpose, an Indian company may be taken as being:

“owned” by resident Indian citizens and Indian companies, which are owned and controlled by resident Indian citizens, if more than 50% of the equity interest in it is beneficially owned by resident Indian citizens and Indian companies, which are owned and controlled ultimately by resident Indian citizens;

“controlled” by resident Indian citizens and Indian companies, which are owned and controlled by resident Indian citizens, if the resident Indian citizens and Indian companies, which are owned and controlled by resident Indian citizens, have the power to appoint a majority of its directors.

If the investing company is owned or controlled by ‘non resident entities’, the entire investment by the investing company into the subject Indian Company would be considered as indirect foreign investment,

For the above purpose, an Indian company may be taken as being:

“owned” by ‘non resident entities’, if more than 50% of the equity interest in it is beneficially owned by non-residents

“controlled” by ‘non resident entities’, if non-residents have the power to appoint a majority of its directors.

II. TECHNICAL/FINANCIAL COLLABORATION

Foreign investment can be taken in the form of technical collaboration/financial collaboration. Financial Collaboration involves Foreign Direct investments in the form of Equity, FCCBs etc and in technical collaboration it involves payment of royalty, technical know-how fee etc. Both forms of investment may take place under automatic route where post facto approval of RBI is obtained when the investment/payments are within the limits. When it exceeds the specified limits, it requires prior approval of central government.

Foreign Direct Investment (Financial Collaboration)

Foreign Direct Investments (FDI) can be made under the following two routes

1. Automatic Route and
2. Government Route/Approval Route.

Under the Automatic Route, the foreign investor or the Indian company does not require any approval from the Reserve Bank or Foreign Investment Promotion Board for the investment.

Under the Government Route, prior approval Foreign Investment Promotion Board (FIPB) is required.

Foreign Direct Investment in India is allowed under automatic route except under the following circumstances.

(i) Proposals that require an industrial licence
(ii) Cases where foreign investment is more than 24% in the equity capital of
units manufacturing items reserved for SSIs.

(iii) Proposals in which the foreign collaborator has a previous venture/tie-up in India.

(iv) Proposals relating to acquisition of shares in an existing Indian Company in favour of Foreign/NRI/OCB investor.

(v) Proposals falling outside notified sectoral caps

(vi) Sectors where FDI is not permitted.

(vii) Investor chooses not to avail automatic route.

Eligibility for Foreign Direct Investment

A person resident outside India (other than a citizen of Pakistan or Bangladesh) or an entity incorporated outside India, (other than an entity incorporated in Pakistan or Bangladesh) can invest in India, subject to the FDI Policy of the Government of India.

Erstwhile OCBs, who have converted themselves into companies incorporated outside India can make fresh investments in India under the FDI Scheme provided they are not under the adverse notice of Reserve Bank / SEBI

Type of Instruments available for Foreign Direct Investment

Equity shares / convertible debentures and preference shares are eligible under Foreign Direct Investment. Other instruments such as preference shares (non-convertible, optionally convertible or partially convertible) are considered as debt and guidelines applicable for External Commercial Borrowing (ECB) will apply to such issues. As far as Debentures are concerned, only those which are fully and mandatorily convertible into equity, within a specified time would be reckoned as part of equity under the FDI Policy.

Technical collaboration (Foreign Technology Agreements)

For promoting technological capability and competitiveness of the Indian Industry, acquisition of foreign technology is encouraged through foreign collaboration agreements. Induction of know-how through such collaborations is permitted either through automatic route or with prior government approval.

(a) Under FEMA Regulations

Payment of foreign technology collaboration by Indian Companies are allowed under automatic route subject to the following limits

1. the lump sum payments not exceeding US$ 2 million
2. Royalty payable is being limited to 5% for domestic sales and 8% for exports, without restriction on duration of royalty payments. The royalty limits are net of taxes and are calculated according to standard conditions.
3. Payment of royalty upto 2% for exports and 1% for domestic sales is allowed under automatic route for use of trademarks and brand name of the foreign collaborator without technology transfer.

(b) Under Competition Act, 2002
(i) **Licencing agreements**

The provisions relating to anti-competitive agreements under the Competition Act, 2002 does not restrict the right of any person, to restrain any infringement of intellectual property rights or to impose such reasonable conditions as may be necessary for the purposes of protecting any of his rights which have been or may be conferred upon him under the following legislations relating to intellectual property rights—

- the Copyright Act, 1957;
- the Patents Act, 1970;
- the Trade and Merchandise Marks Act, 1958 or the Trade Marks Act, 1999;
- the Geographical Indications of Goods (Registration and Protection) Act, 1999;
- the Designs Act, 2000;

These, Intellectual property legislations confer exclusive rights on holders of patents, copyright, design rights, registered trademarks and other related rights protected by law. A holder of intellectual property rights is authorised to prevent any unauthorized used of its intellectual property and to exploit such property, in particular by licensing it to third parties. Thus, the technology transfer agreements which involves licensing of technology are outside the purview of Section 3 prohibition. It is presumed that such agreements usually improve economic efficiency and are pro-competitive as they can reduce duplication of research and development, strengthen the incentive for the initial research and development, spur incremental innovation, facilitate diffusion and generate product market competition.

However, licensing agreements may also be used for anti-competitive purposes, e.g. where two competitors use a licensing agreement to share out markets between themselves or where an important licence holder excludes competing technologies from the market.

(ii) **Joint Venture Agreements**

It has been clarified that any agreement entered into by way of joint ventures shall not be prohibited by Section 3(1) of Competition Act, 2002 if such agreements increase efficiency in production, supply, distribution, storage, acquisition or control of goods or provisions of services.

III. **JOINT VENTURES IN INDIA**

Joint Ventures and Foreign Collaborations are important business models which become more popular with the opening up of the economies in the context of liberalization, competition and globalization.

A joint venture is a partnership through which two or more firms create a separate entity to carry out a particular economic activity in which each partner takes an active role in decision making. The essential features of joint ventures may be classified as:
(a) an agreement between the parties on common long term objectives such as production, sales, financing etc.

(b) pooling of assets, IPRs and other facilities for achievement of agreed objectives

(c) sharing of profits.

Joint ventures are considered appropriate when complementary needs exist between companies and there is compatibility with the strategies.

Joint Venture (JV) and Wholly Owned Subsidiary have been defined in the Foreign Exchange Management (Transfer and Issue of Foreign Security) Regulations, 2000 as under:

Joint Venture (JV) means a foreign entity formed, registered or incorporated in accordance with the laws and regulations of the host country in which the Indian party makes a direct investment

In recent years, the term "joint venture" has also been used interchangeably with a newer business vehicle called the "strategic alliance".

A strategic alliance is a specific form of collaboration between two or more companies. Strategic alliances with stronger overseas partners can provide a means of overcoming the problems of small size and lack of resources faced by some companies.

Features of a joint venture

Besides the requirement that a joint venture must have a contractual basis, there are certain additional requisites for the successful existence of a joint venture. Although its existence depends on the facts and circumstances of each particular case, generally the following factors must be present:

(a) Contribution by the parties in the form of money, property, effort, knowledge, skill and other assets to a common understanding;

(b) a joint property interest in the subject matter of the venture;

(c) a right of mutual control or management of the enterprise;

(d) expectation of profit;

(e) a right to participate in the profits;

(f) most usually, limitation of the objective to a single undertaking; and

(g) clear understanding of formation, performance and exit mechanism between joint venture parties.

How Does a Joint Venture Work?

— A successful joint venture is one where each partner contributes complementary skills and resources in an ongoing relationship offering mutual benefits.

— Much depends on what the two parties have to offer each other, and how these assets can be put together in a workable business structure.
While there is no set formula for putting together a joint venture, a typical arrangement might be as follows:

1. One of the partners contributes, manufacturing technology, product know-how, patents (if any), business expertise, technical training and management.
2. The partner in the market may contribute an existing plant and facilities, local management and staff, knowledge of the local market (including distribution and sales resources), and relationships with the government, financial institutions and other groups.
3. Both partners contribute capital to establish the venture, ongoing financial support, responsibility for marketing key management decisions.

This would be particularly appropriate for joint ventures in developing countries where technology transfer is the major benefit sought by the local economy. The export of finished goods or materials may or may not be part of this package. By building a structure that reinforces each other’s respective strengths, and creating synergy, a better overall result is obtained than could be achieved by each partner independently.

Preliminary considerations

— **Selection**: Selection of an appropriate co-venturer can have long lasting implications for the operation and success of the venture as the ability of the co-managing parties to co-exist and make unanimous decisions is essential to the success of a joint venture. The potential parties should identify their mutual interest and establish a common objective.

— **Setting out the objectives and expectations**: Setting out the objectives and expectations of the venture is pre-requisite. It is essential that the nature, scope and duration of the joint venture be identified.

— **Employ competent professionals**: Competent professionals like CS, Legal experts experienced in drafting joint venture and strategic alliance agreements should be retained as consultants, to structure the deal with proper legal advice. Professionals can assist the parties to structure a legal agreement which reflects the deal and properly addresses the subject matter and should be able to assist the parties in understanding their strengths, intentions and problems and in ensuring that the parties’ goals are compatible. They can also structure an agreement which can assist the parties in terminating the relationship with minimal disruption.

— **Negotiation**: It is appropriate that negotiations be conducted at the level of more senior management. It is desirable to have negotiating teams consisting of senior management together with management responsible for implementing the alliance. This will assist in establishing the requisite internal consensus.

— **Attitude**: Negotiations for alliances should not be entered into with an adverse approach to the opposing party. This is never productive or efficient in the negotiation of any normal commercial arrangement. Adversarial negotiations when entering into strategic alliance and joint venture
agreements is always' disruptive and counterproductive.

— **MOU:** The next step is to prepare memorandum of understanding, setting out the objectives of the joint venture prior to finalising the joint venture agreement. The MOU may set out the key features of the proposed joint venture arrangements and can represent a broad outline of the definitive agreement. In addition to prescribing fundamental business terms, the MOU often provides for at least two other binding commitments, namely, for the exclusivity of negotiations for a stated period of time and confidentiality.

— **Due Diligence:** After the parties have agreed on the basic terms of the joint venture arrangement a fixed period of time is often set in which to conduct a detailed and comprehensive review of all information pertinent to the proposed business venture prior to the execution of the joint venture agreement. This process is referred to as "due diligence". In technology-driven industries and other industries where intellectual property is an important element of the joint venture due diligence plays an essential role in evaluating the technology and intellectual property assets and assessing their validity.

### Reasons for entering into a joint venture

Parties looking for an appropriate business vehicle often seek out a joint venture arrangement because of the benefits it affords with respect to the limitation of liability of the parties to the venture. The reasons for creating a joint venture could be stated as the ability to combine the strengths, expertise, technology, and know-how of separate businesses with a sharing of investment costs and risks.

The following list is a summary of other motivations for entering into a joint venture:

— A company may want to enter into a foreign market with which it is not familiar.

— The joint venture allows the parties to the venture to undertake a potentially speculative and high-risk endeavour without exposing assets to unlimited liability.

— The joint venturing parties can define at the outset of the project, the extent to which each shall be liable for costs and how the risks associated with the venture shall be allocated.

— A joint venture can offer flexibility in distributing operational responsibilities authority and facilitate use of the strengths of each party to the venture.

— A joint venture may be entered into for competitive considerations for example a joint venture with a potential competitor may reduce or eliminate competition.

### Benefits of Joint Venture

— Sharing of risks;

— Access to technology/ R &D/markets;

— Access to foreign capital;
— Reduction of manufacturing costs and other overheads including expenditure on R & D;
— Complimentary skills/resources;
— New technology or products or capital.
— To kill competition.

Risk involved

A joint venture involves co-ownership and co-management. This may result in disturbance in consultative decision-making. This is particularly true with respect to joint ventures where there is 50/50 ownership and/or control. This type of ownership or management structure lends itself to an increasing risk of deadlock amongst decision-makers. However, it is possible for parties contemplating entering into a joint venture to anticipate these decision-making hurdles and to provide safeguards or procedures to be followed to ensure that conflict amongst the participants in the venture does not paralyse the operation of the joint venture.

Critical Success Factors

Followings are the key factors in successful JV operation:

— Rapport between the two partners - get to know each other and fully recognise, understand and accept the other's requirements in advance.
— Communication channels must be kept open and agreed reporting timetables and format adhered to.
— Positive results for both partners with a reasonable and agreed timeframe.

One of the key attractions of joint ventures is their flexibility. They can be moulded and shaped in a variety of ways to suit the specific needs of the partners and of the markets. It is common to enter into a joint venture after tried other options such as on consortium arrangement etc., or many a casts, successful joint ventures are formed with known suppliers and subcontractors.

Disadvantages of a Joint Venture

— Potentially high capital cost plus ongoing financial support are required
— Profitable returns may take some time to achieve
— High level of commitment of staff and management takes time
— Time consuming (especially where a new venture is involved)
— Potential for conflict between joint venture partners
— Cultural differences and communications difficulties
— A minority equity position may work against partner
— Difficult to get out of it quickly, if desired
— Working in a different legal and commercial system
— Political risks in the country where the joint venture is based
Laws Applicable
— Companies Act, 1956;
— Partnership Act;
— Policy for Foreign Investment (FEMA Regulations); MRTP,
— Industrial Policy and procedures; SEBI Guidelines; contract Act etc.
— Competition Act, 2002
— Foreign Trade (Development and Regulation) Act, 1992

Structuring of JV
— Identify Strategic & Operational issues,
— Execution of MOU/ Principle terms,
— Due-diligence (legal & financial),
— Documentation

1. Strategic issues
— To define objectives (whether the JV would be manufacturing, or simply marketing);
— Key support from the Partners, on what terms?
— Key decisions how to be taken and implemented.

2. Operational Issues
— Day-to-day management rights,
— internal policy systems including reporting requirements,
— Audit and information rights.
— Deliberate and agree upon all strategic and operational issues;

3. Execute a formal Memorandum of Understanding/Principle terms of agreement, to cover at least,
— Objective of the JV,
— Broad form of partnership;
— Identify a way forward in the event of disagreement on any issue before closing.

4. Carry out due-diligence on the following:
— Company's background and history,
— Financial, Tax and Accounting,
— Manufacturing, Marketing & Distribution,
— Major contracts, licenses and approvals,
— Corporate compliance,
— Litigations by or against the company,
— Ownership of assets including intellectual property.
— Borrowings/loan documents.
— IPR

**Steps to a Joint Venture**

1. Recognise your options - Identify different methods that can be adopted for entering into the venture

2. Determine the resources you can commit
   — Time
   — Money
   — People

3. Select and understand your market
   — Consumer research to pinpoint the opportunities
   — Comprehensive assessment of the investment and legal environment to justify the risks and establish the costs of the proposed joint venture.

4. Determine a joint venture strategy
   — What type of joint venture
   — Where
   — With whom
   — What time-frame
   — How much will it cost

5. Determine the objectives of the joint venture
   — What do you hope to gain from the joint venture?
   — What does your partner hope to gain?
   — What will the joint venture actually do?

6. Select a Partner
   — Identify USP (Unique setting points) of both the parties
   — Compatibility is crucial
   — Take time to get to know each other
   — Understand each other's expectations

7. Exchange letters

8. Feasibility study:

   (a) Establish a business structure
   — What legal structure will the joint venture have - incorporated, unincorporated?
— How will it work?
— What is the equity basis?
— Who is responsible for what?
— What needs to be put in place?

(b) Resolve investment and legal issues - often a time consuming process
— What rules and approvals must the joint venture comply with?
— What tax implications are there?
— How will the profits be remitted back.

(c) Evaluate potential investment sites
— Physical location of joint venture
— What purchases will need to be made - land, buildings, equipment

(d) Jurisdictions?

(e) Dispute resolution mechanism.

9. Agreement in Principle
10. Negotiation
11. Finalising major points to be covered in the Agreement - Performance Targets and Exit Clauses - it is important to think about these at the beginning of the relationship when you and your partner are on good terms.
12. Joint Venture Agreement
13. Staged implementation
14. Full operationalisation
15. Review
16. Expansion, if any
17. Steps if the Joint Venture Runs into Difficulties
   — Arbitration
   — Quitting
   — Dissolution

IV. SAMPLE CHECK-LIST ON JOINT VENTURES IN INDIA

Checklist – Financial Collaboration

Joint Venture in India can be either by setting up a new company or by investing into an existing company.

In either case, the following check list (not exhaustive) has to be looked into:

1. Check FEMA Provisions for investment in India i.e. Foreign Direct Investment Policy as well as FEMA Regulations. Investment in India is regulated by Reserve Bank of India through Notifications, Circulars and Press Notes within
the broad framework of the FDI Policy.

(a) **Prohibited Sectors:** RBI has specified certain sectors where investment is prohibited.

(b) **Automatic Route:** Foreign Direct Investment is allowed in almost all sectors under Automatic route, within sectoral caps prescribed. RBI has prescribed Form FC-GPR for reporting shares issued to the Foreign Investors by an Indian company, not later than 30 days from the date of issue of shares.

(c) **Approval Route:** Investment which does not qualify under Automatic route, has to go for government approval.

Further, where such investment does not conform to policies of Government of India, a specific approval from Government must be sought. For example, there are Government guidelines on location of industrial units, or there are certain items like explosives or liquor that need an industrial licence. If the Indian company does not conform to the locational guidelines or small scale policy or needs an Industrial licence or investment beyond sectoral cap, then it cannot issue shares under the Automatic Route. If for any of the reasons mentioned above, the Indian company cannot issue shares to foreign investors under the Automatic Route, an application may be made to Secretariat for Industrial Assistance (SIA), Ministry of Commerce & Industry, Government of India, Udyog Bhavan, New Delhi or Foreign Investment Promotion Board (FIPB). (Form FC-IL has been prescribed for this purpose. However, a plain paper application is also accepted). If the unit is located in any of the Export Processing Zones, applications should be made to the Development Commissioner of the Export Processing Zone concerned.

2. Check whether Board resolution under section 292 as well as authorizing the Board to enter into Agreement and obtaining approvals from RBI/FIPB, as applicable has been passed

3. Check whether General Meeting resolution as required under Section 372A has been passed for inter-corporate investments, if required.

4. Check joint venture agreement is drafted meticulously

5. In case a new Company is being set up in India, the following steps has to be followed:
   1. Check Board resolution of the body corporate established abroad.
   2. Check the Constitution of the body corporate
   3. Check the Confirmation of inward remittance of the body corporate's shareholding amount
   4. Check the incorporation and other procedural matters.

6. In case the investment to be made in India is in an existing company:
   1. Check the Board resolution of the body corporate established abroad.
   2. Check the Constitution of the body corporate
3. Check the Confirmation of inward remittance of the body corporate's shareholding amount

4. In case fresh allotment of shares is being made, applicable Companies Act provisions and related SEBI guidelines as applicable FEMA regulations, are required to be complied with.

5. In case transfer of shares is being made to the body corporate abroad, check that the transfer of shares guidelines specified in Notification No. FEMA 20/2000-RB dated 3rd May, 2000 as amended from time to time, are complied with. Obtain certificate from the Authorised Dealer in Form FC-TRS and record the details in the company's register of transfers.

6. If there is a substantial acquisition of shares by the body corporate abroad in the Indian company, the SEBI takeover code also needs to be complied with.

7. Check whether the Indian Company has reported the particulars of foreign inward remittance within 30 days of its receipt.

8. Check whether the allotment is made within 180 days of inward remittance.

9. Check whether the Company has filed form FC-GPR within 30 days of allotment.

Technical Collaboration – Check List

1. Check the Board Resolution authorising the board to enter into agreement.

2. Check various clauses of technical collaboration agreement including clauses relating to Intellectual property rights.

3. Check board resolution of body corporate situated outside India.

4. Check whether necessary approval from RBI/SIA has been obtained by filing forms FT/FC/IL as the case may be.

5. Check for Royalty remittances and the necessary RBI filings in this regard.

V. SETTING UP OF BRANCH, LIAISON, PROJECT OFFICES

Foreign Companies can set up their operations in India through

— Liaison Office/Representative Office
— Project Office
— Branch Office

Liaison office acts as a channel of communication between the principal place of business or head office and Indian activities. Liaison office can not undertake any commercial activity directly or indirectly and can not, therefore, earn any income in India. Its role is limited to collecting information about possible market opportunities and providing information about the company and its products to prospective Indian
customers. It can promote export/import from/to India and also facilitate technical/financial collaboration between parent company and companies in India. Approval for establishing a liaison office in India is granted by Reserve Bank of India (RBI).

Foreign Companies planning to execute specific projects in India can set up temporary project/site offices in India. RBI has now granted general permission to foreign entities to establish Project Offices subject to specified conditions. Such offices can not undertake or carry on any activity other than the activity relating and incidental to execution of the project. Project Offices may remit outside India the surplus of the project on its completion, general permission for which has been granted by the RBI.

Foreign companies engaged in manufacturing and trading activities abroad are allowed to set up Branch Offices in India for the following purposes:

- Export/Import of goods
- Rendering professional or consultancy services
- Carrying out research work, in which the parent company is engaged.
- Promoting technical or financial collaborations between Indian companies and parent or overseas group company.
- Representing the parent company in India and acting as buying/selling agents in India.
- Rendering services in Information Technology and development of software in India.
- Rendering technical support to the products supplied by the parent/group companies.

It may be noted that retail trading activities of any nature is not allowed for a branch office in India.

A branch office is not allowed to carry out manufacturing activities on its own but is permitted to subcontract these to an Indian manufacturer. Branch Offices established with the approval of RBI, may remit outside India profit of the branch, net of applicable Indian taxes and subject to RBI guidelines, permission for setting up branch offices is granted by the Reserve Bank of India (RBI).

No approval shall be necessary from RBI for a company to establish a branch/unit in SEZs to undertake manufacturing and service activities subject to specified conditions.

Such Branch Offices would be isolated and restricted to the Special Economic Zone (SEZ) alone and no business activity/transaction will be allowed outside the SEZs in India, which include branches/subsidiaries of its parent office in India.

Application for setting up Liaison Office/Project Office/Branch Office may be submitted in form FNC 1, along with the following documents:

- English version of the Certificate/Registration or Memorandum and Articles of Association attested by Indian Embassy/Notary Public in the country of Registration.
— Latest Audited Balance Sheet of the applicant entity.

**LESSON ROUND-UP**

- Foreign investment in India is governed by Foreign Direct Investment Policy and sub-section (3) of section 6 of the Foreign Exchange Management Act, 1999 read with Notification No. FEMA 20/2000-RB dated May 3, 2000, containing Foreign Exchange Management (Transfer or issue of security by a person resident outside India) Regulations, 2000 which has been amended from time to time.
- Foreign investment in India is freely permitted in almost all sectors except for specified prohibited sectors.
- Foreign Direct Investments (FDI) can be made under Automatic Route and Government Route/Approval Route.
- Joint Venture in India can be either by setting up a new company or in an existing company.

**SELF-TEST QUESTIONS**

1. Explain the possible entry routes for foreign investments in India?
2. Describe the points to be checked in case of foreign direct investment through automatic route.
3. What are the steps involved in joint ventures?
4. Elaborate the points to be checked while setting up a joint venture in India?
5. Write a note on setting up branch, liaison and project office in India.
I. INTRODUCTION AND STATUTORY BASIS

Setting up of wholly owned subsidiaries (WOS) and Joint Ventures abroad is a Direct Investment which may take in the form of newly promoted foreign concerns or additional investment by Indian parties in the existing foreign concerns or investment for acquisition of overseas business.

Outbound Investment or Direct Investment outside India includes investment made by Indian Parties by way of contribution to the capital or subscription to the Memorandum of Association of foreign entity, setting up of joint ventures or wholly owned subsidiaries in overseas, direct investment under swap or exchange of shares arrangement, capitalization of exports, acquisition of a foreign company through tender procedure. Besides equity stake, Joint ventures may be reflected in the form of representation in the Board of foreign entity, supply of technical know how, capital goods etc to the foreign concern.

Investment in foreign securities is a permissible capital account transaction under schedule I of Foreign Exchange Management (Permissible Capital Account Transactions) Regulations, 2000.

Setting up of WOS and Joint Ventures requires compliance with various laws in India and the laws and regulations of host country. In India, it is mainly regulated by Foreign Exchange Management (Transfer or Issue of Any Foreign Security) Regulations, 2004 and amendments there on in addition to Companies Act, 1956, FEMA, 1999 and other relevant Acts. Following are the important definitions under the said regulations.

‘Direct Investment outside India’ means investment by way of contribution to the capital or subscription to the Memorandum of Association of a foreign entity or by way of purchase of existing shares of a foreign entity whether by market purchase or private placements or through stock exchanges, but does not include portfolio investment.
'Joint Venture’ mean a foreign entity formed registered or incorporated in accordance with the laws and regulations of the host country in which the Indian Party makes a direct investment.

‘Wholly owned subsidiary’ means a foreign entity formed, registered or incorporated in accordance with the laws and regulation of the host country whose entire capital is hold by Indian party.

II. ELIGIBILITY

An Indian party is eligible to make direct investment in Joint Venture or Wholly Owned Subsidiary outside India. As per Foreign Exchange Management (Transfer or Issue of Any Foreign Security) Regulations, 2004 Indian party includes

(i) A company incorporated in India
(ii) Body created under an Act of Parliament
(iii) Partnership Registered under Indian Partnership Act, 1932
(iv) Any other entity as may be notified by the Reserve Bank

In case of partnership, individual partner can hold foreign securities for and on behalf of the firm, only if host country regulations or operational requirements warrant such holding.

III. RESTRICTIONS/PROHIBITIONS

(a) Indian parties are prohibited from making direct investment in a foreign entity engaged in real estate /banking business. It may be noted that Indian Banks operating in India can set up WOS abroad, provided they obtain clearance under Banking Regulation Act, 1949.

(b) Investment in Pakistan is not permitted under Automatic Route

(c) A person resident in India is not permitted to make Overseas Direct Investments unless RBI’s prior approval is obtained. However he may purchase a foreign security out of funds held in Resident Foreign Currency (RFC) account maintained in accordance with the Foreign Exchange Management (Foreign Currency Accounts) Regulations, 2000.

IV. APPROVALS REQUIRED

(a) Approval from Board of Directors
(b) Shareholders of the Company
(c) Approval from Department of Economic Affairs, Ministry of Finance, if required
(d) Approval from Reserve Bank of India (pre/post facto)

V. DIRECT INVESTMENT OUTSIDE INDIA- AUTOMATIC ROUTE

(a) Limits and Conditions

According to Regulation 6 of Foreign Exchange Management (Transfer or issue of any Foreign Security) Regulations, 2000, an Indian party is permitted to make investment in overseas Joint Ventures (JV) / Wholly Owned Subsidiaries (WOS), not
exceeding 400 per cent of its net worth as on the date of the last audited balance sheet. However, the ceiling of 400 per cent of net worth will not be applicable where the investment is made out of balances held in Exchange Earners' Foreign Currency account of the Indian party or out of funds raised through ADRs/GDRs. The Indian party is required to approach an Authorised Dealer Category - I bank with an application in Form ODI and prescribed enclosures / documents for effecting remittances towards such investments. Such overseas investments will include contribution to the capital of the overseas JV / WOS, loan granted to the JV / WOS and 100 per cent of guarantees issued to or on behalf of the JV/WOS.

It may be noted that Applications for investment in JV/WOS overseas in the energy and natural resources sectors (e.g. oil, gas, coal and mineral ores) in excess of 400 per cent of the net worth of the Indian companies as on the date of the last audited balance sheet may be considered by RBI and accordingly AD Category - I banks may forward such applications from their constituents to the Reserve Bank as per the laid down procedure.

These investments are subject to the following conditions:

(i) The Indian entity may extend loan / guarantee to an overseas concern only in which it has equity participation. Indian entities may offer any form of guarantee - corporate or personal / primary or collateral / guarantee by the promoter company / guarantee by group company, sister concern or associate company in India; provided that

1. All financial commitments including all forms of guarantees are within the overall ceiling prescribed for overseas investment by the Indian party i.e. currently within 400 per cent of the net worth of the Indian party,
2. No guarantee is ‘open ended’ i.e. the amount of the guarantee should be specified upfront, and
3. As in the case of corporate guarantees, all guarantees are required to be reported to Reserve Bank, in Form ODI-Part II. Guarantees issued by banks in India in favour of WOSs / JVs outside India, would be outside this ceiling and would be subject to prudential norms issued by Reserve Bank from time to time.

It may be noted that Specific approval of the Reserve Bank will be required for creating charge on immovable property and pledge of shares of the Indian parent/ group companies in favour of a non-resident entity.

(ii) The Indian party should not be on the Reserve Bank’s Exporters caution list / list of defaulter to the banking system circulated by the Reserve Bank / Credit Information Bureau (India) Ltd (CIBIL) / or any other Credit Information company as approved by the Reserve Bank or under investigation by any investigation / enforcement agency or regulatory body.

(iii) All transactions relating to a JV / WOS should be routed through one branch of an authorised dealer bank to be designated by the Indian party.

(iv) In case of partial / full acquisition of an existing foreign company, where the investment is more than USD 5 million, valuation of the shares of the company shall be made by a Category I Merchant Banker registered with SEBI or an Investment Banker / Merchant Banker outside India registered
with the appropriate regulatory authority in the host country; and, in all other cases by a Chartered Accountant or a Certified Public Accountant.

(v) In cases of investment by way of swap of shares, irrespective of the amount, valuation of the shares will have to be by a Category I Merchant Banker registered with SEBI or an Investment Banker outside India registered with the appropriate regulatory authority in the host country. Approval of the Foreign Investment Promotion Board (FIPB) will also be a prerequisite for investment by swap of shares.

(vi) In case of investment in overseas JV / WOS abroad by a registered Partnership firm, where entire funding for such investment is done by the firm, it will be in order for individual partners to hold shares for and on behalf of the firm in the overseas JV / WOS if the host country regulations or operational requirements warrant such holdings.

(vii) Investments in JV/WOS abroad by Indian parties through the medium of a Special Purpose Vehicle (SPV) is also permitted under the Automatic Route subject to the conditions that the Indian party is not included in the Reserve Bank’s Caution list or is under investigation by the Enforcement Directorate or included in the list of defaulters to the banking system circulated by the Reserve Bank/any other Credit Information company as approved by the Reserve Bank Indian parties whose names appear in the Defaulters’ list require prior approval of the Reserve Bank for the investment. It is clarified that setting up of an SPV under the Automatic Route is permitted only for the purpose of investment in JV/WOS overseas.

(viii) An Indian party may acquire shares of a foreign company engaged in a bonafide business activity, in exchange of ADRs/GDRs issued to the latter in accordance with the Scheme for issue of Foreign Currency Convertible Bonds and Ordinary Shares (through Depository Receipt Mechanism) Scheme, 1993, and the guidelines issued there under from time to time by the Central Government, provided:

(1) ADRs/GDRs are listed on any stock exchange outside India;
(2) The ADR and/or GDR issue for the purpose of acquisition is backed by underlying fresh equity shares issued by the Indian party;
(3) The total holding in the Indian entity by persons resident outside India in the expanded capital base, after the new ADR and/or GDR issue, does not exceed the sectoral cap prescribed under the relevant regulations for such investment under FDI;
(4) Valuation of the shares of the foreign company shall be
   (a) as per the recommendations of the Investment Banker if the shares are not listed on any recognized stock exchange; or
   (b) based on the current market capitalisation of the foreign company arrived at on the basis of monthly average price on any stock exchange abroad for the three months preceding the month in which the acquisition is committed and over and above, the premium, if any, as recommended by the Investment Banker in its due diligence report in other cases.

The Indian Party is required to report such acquisition in form ODI to the AD
Bank for report to the Reserve Bank within a period of 30 days from the date of the transaction. It may be noted that Investments in Nepal are permitted only in Indian rupees. Investments in Bhutan are permitted in Indian Rupees as well as in freely convertible currencies. All dues receivable on investments made in freely convertible currencies, as well as their sale / winding up proceeds are required to be repatriated to India in freely convertible currencies only. The automatic route facility is not available for investment in Pakistan.

(b) Investment in Unincorporated entities Overseas in oil sector under the Automatic Route

(1) Investments in unincorporated entities overseas in the oil sector (i.e. for exploration and drilling for oil and natural gas, etc.) by Navaratna PSUs, ONGC Videsh Ltd. (OVL) and Oil India Ltd.(OIL) may be permitted by AD Category - I banks, without any limit, provided such investments are approved by the competent authority.

(2) Other Indian companies are also permitted under the Automatic Route to invest in unincorporated entities overseas in the oil sector up to 400 per cent of its net worth provided the proposal has been approved by the competent authority and is duly supported by certified copy of the Board resolution approving such investment. Investment in excess of 400 per cent of the net worth of an Indian company shall require prior approval of the Reserve Bank.

(c) Capitalisation of exports and other dues

Indian parties are permitted to capitalise the payments due from the foreign entity towards exports, fees, royalties or any other dues from the foreign entity for supply of technical knowhow, consultancy, managerial and other services within the ceilings applicable. Capitalisation of export proceeds remaining unrealised beyond the prescribed period of realization will require prior approval of the Reserve Bank.

Indian software exporters are permitted to receive 25 per cent of the value of their exports to an overseas software start-up company in the form of shares without entering into Joint Venture Agreements, with prior approval of the Reserve Bank.

(d) Investments in Financial Services Sector

According to Regulation 7 of Foreign Exchange Management (Transfer or Issue of any Foreign Security) Regulations, 2000, Indian party seeking to make investment in an entity engaged in the financial sector should fulfill the following additional conditions:

(i) be registered with the appropriate regulatory authority in India for conducting the financial sector activities;

(ii) have earned net profit during the preceding three financial years from the financial services activities;

(iii) have obtained approval for investment in financial sector activities abroad from regulatory authorities concerned in India and abroad; and

(iv) have fulfilled the prudential norms relating to capital adequacy as prescribed by the regulatory authority concerned in India.

It may be noted that a step down subsidiary of JV / WOS investing in a financial sector.
services sector is also required to comply with the above conditions.

Trading in Commodities Exchanges overseas and setting up JV/WOS for trading in overseas exchanges will be reckoned as financial services activity and require clearance from the Forward Markets Commission.

(e) Method of Funding

(1) Investment in an overseas JV / WOS may be funded out of one or more of the following sources:
   (i) drawal of foreign exchange from an AD Bank in India;
   (ii) capitalisation of exports;
   (iii) swap of shares
   (iv) utilisation of proceeds of External Commercial Borrowings (ECBs) / Foreign Currency Convertible Bonds (FCCBs);
   (v) in exchange of ADRs/GDRs issued in accordance with the scheme for issue of Foreign Currency Convertible Bonds and Ordinary Shares (through Depository Receipt Mechanism) Scheme, 1993, and the guidelines issued there under from time to time by the Central Government
   (vi) balances held in EEFC account of the Indian party; and
   (vii) utilisation of proceeds of foreign currency funds raised through ADR / GDR issues.

   In respect of (vi) and (vii) above, the ceiling of 400 per cent of net worth will not apply. In respect of investments in the financial sector, they will be subject to compliance of Regulation 7 which has already been discussed in the previous paragraphs.

   (2) General permission has been granted to residents for purchase / acquisition of securities in the following manner
   (i) out of funds held in RFC account;
   (ii) as bonus shares on existing holding of foreign currency shares; and
   (iii) when not permanently resident in India, out of their foreign currency resources outside India

VI. DIRECT INVESTMENT OUTSIDE INDIA – APPROVAL ROUTE

All applications of Direct Investment outside India which are not qualifying for Automatic route as mentioned in the above mentioned paragraphs are required to obtain prior approval from Reserve Bank of India.

VII. ACQUISITION OF A FOREIGN COMPANY THROUGH BIDDING OR TENDER PROCEDURE

An Indian party may remit earnest money deposit or issue a bid bond guarantee for acquisition of a foreign company through bidding and tender procedure and also make subsequent remittances through an Authorised Dealer Category - I bank, in accordance with the provisions of Regulation 14 of Foreign Exchange Management
In terms of the said Regulation 14, Authorised Dealer Category – I (AD) banks may, on being approached by an eligible Indian party and subject to the limits, allow remittance towards Earnest Money Deposit (EMD) to the extent eligible after obtaining Form A2 duly filled in or may issue bid bond guarantee on their behalf for participation in bidding or tender procedure for acquisition of a company incorporated outside India. On winning the bid, AD banks may remit the acquisition value after obtaining Form A2 duly filled in and report such remittance (including the amount initially remitted towards EMD) to the Chief General Manager, Foreign Exchange Department, Central Office, Overseas Investment Division, Amar Building, 5th floor, Mumbai 400 001 in form ODI. AD Category – I banks, while permitting remittance towards EMD should advise the Indian party that in case they are not successful in the bid, they should ensure that the amount remitted is repatriated in accordance with Foreign Exchange Management (Realisation, Repatriation & Surrender of Foreign Exchange) Regulations, 2000.

In cases where an Indian party, after being successful in the bid / tender decides not to proceed further with the investment, AD banks should submit full details of remittance allowed towards EMD / invoked bid bond guarantee, to the Chief General Manager, Foreign Exchange Department, Central Office, Overseas Investment Division, Amar Building, 5th floor, Mumbai 400 001.

In case the Indian party is successful in the bid, but the terms and conditions of acquisition of a company outside India are not in conformity with the provisions of Regulations, or different from those for which specific approval has already been obtained from RBI, the Indian entity should again obtain approval from the Reserve Bank by submitting form ODI.

VIII. INVESTMENT UNDER SWAP OR EXCHANGE OF SHARES ARRANGEMENTS

In cases of investment by way of swap of shares, irrespective of the amount, valuation of the shares will have to be by a Category I Merchant Banker registered with SEBI or an Investment Banker outside India registered with the appropriate regulatory authority in the host country. Further, approval of the Foreign Investment Promotion Board (FIPB) will also be a prerequisite for investment by swap of shares.

AD Category – I banks are additionally required to submit to the Reserve Bank the details of transactions such as number of shares received / allotted, premium paid / received, brokerage paid / received etc., and also confirmation to the effect that the inward leg of transaction has been approved by FIPB and the valuation has been done as per laid-down procedure and that the overseas company’s shares are issued / transferred in the name of the Indian investing company. AD Category – I bank may also obtain an undertaking from the applicants to the effect that future sale/transfer of shares so acquired by Non-Residents in the Indian company shall be in accordance with the provisions of Notification No. FEMA 20/2000-RB dated May 3, 2000 as amended from time to time(i.e Foreign Exchange Management(Transfer or Issue of Security by a person Resident outside India) Regulations, 2000.

IX. OVERSEAS INVESTMENTS BY PROPRIETORSHIP CONCERNS/UNREGISTERED PARTNERSHIP
With a view to enabling recognized star exporters with a proven track record and a consistently high export performance to reap the benefits of globalization and liberalization, proprietorship concerns and unregistered partnership firms are allowed to set up a JV / WOS outside India with prior approval of the Reserve Bank subject to satisfying certain eligibility criteria.

An application in form ODI may be made to the Chief General Manager, Reserve Bank of India, Foreign Exchange Department, Overseas Investment Division, Central Office, Amar Building 5th Floor, Fort, Mumbai 400 001, through the AD Category - I bank. AD Category - I banks may forward the applications to the Reserve Bank along with their comments and recommendations, for consideration.

Investments by established proprietorship or unregistered partnership exporter firms will be subject to the following conditions:

(i) The Partnership / Proprietorship firm is a DGFT recognized Star Export House.

(ii) The AD Category – I bank is satisfied that the exporter is KYC (Know Your Customer) compliant, is engaged in the proposed business and meets the requirement as indicated at i) above.

(iii) Exporter has proven track record i.e. export outstanding does not exceed 10 per cent of the average export realization of preceding three financial years.

(iv) The exporter has not come under adverse notice of any Government agency like Enforcement Directorate, CBI and does not appear in the exporters' caution list of the Reserve Bank or in the list of defaulters to the banking system in India.

(v) The amount of investment outside India does not exceed 10 per cent of the average of three financial years export realization or 200 per cent of the net owned funds of the firm, whichever is lower.

X. OVERSEAS INVESTMENT BY REGISTERED TRUST / SOCIETY

Registered Trusts and Societies engaged in manufacturing / educational sector / set up hospital in India are allowed make investment in the same sector(s) in a Joint Venture or Wholly Owned Subsidiary outside India, with the prior approval of the Reserve Bank. Trusts/Societies satisfying the eligibility criteria as given below may submit the application/s in Form ODI-Part I, through their AD Category - I bank/s, to the Chief General Manager, Reserve Bank of India, Foreign Exchange Department, Overseas Investment Division, Central Office, Amar Building, 5th Floor, Fort, Mumbai 400 001, for consideration.

Eligibility Criteria:

(a) Trust

(i) The Trust should be registered under the Indian Trust Act, 1882;

(ii) The Trust deed permits the proposed investment overseas;

(iii) The proposed investment should be approved by the trustee/s;

(iii) The AD Category – I bank is satisfied that the Trust is KYC (Know Your Customer) compliant and is engaged in a bonafide activity;
(iv) The Trust has been in existence at least for a period of three years;
(v) The Trust has not come under the adverse notice of any Regulatory / Enforcement agency like the Directorate of Enforcement, CBI etc.

(b) Society
(i) The Society should be registered under the Societies Registration Act, 1860.
(ii) The Memorandum of Association and rules and regulations permit the Society to make the proposed investment which should also be approved by the governing body / council or a managing / executive committee.
(iii) The AD Category - I bank is satisfied that the Society is KYC (Know Your Customer) compliant and is engaged in a bonafide activity;
(iv) The Society has been in existence at least for a period of three years;
(v) The Society has not come under the adverse notice of any Regulatory / Enforcement agency like the Directorate of Enforcement, CBI etc.

In addition to the registration, the activities which require special license / permission either from the Ministry of Home Affairs, Government of India or from the relevant local authority, as the case may be, the AD Category – I bank should ensure that such special license / permission has been obtained by the applicant.

XI. PROCEDURAL CHECKLISTS

(a) Automatic Route

1. Board Resolution is required to be passed under Section 292 of the Companies Act, 1956, specifying the limits for investment by Directors, in respect of out bound investment by the company.

2. Special Resolution has to be passed under Section 372 A of the Companies Act, 1956 for investments in excess of 60% of the paid-up Capital and free reserves or 100% of free reserves whichever is higher and necessary e-form 23 has to be filed with ROC, in case of out bound investment by company.

3. It has to be ensured that direct investment outside India does not exceed 400% of the net worth of the company.

4. Statutory Auditors certificate has to be obtained in the specified format.

5. Valuation report has to be obtained from a Chartered Accountant or certified public accountant. In case the investment is more than USD 5 Million, then valuation has to be done by a category I Merchant Banker registered with SEBI or appropriate authority of the host country.

6. Certificate from Chartered accountant has to be obtained for the reasonableness of the acquisition price.

7. Authorised dealer has to be approached with form A-2, Board Resolution, Statutory Auditors’ certificate etc for effecting the investment.

8. It has to be ensured that Reporting of ODI has to be made in form ODI (both Part I and Part II) with through authorized dealer to The Chief General Manager,
Reserve Bank of India, Foreign Exchange Department, Overseas Investment Division, Amar Bldg. 5th floor, Sir P. M. Road, Fort, Mumbai 400001 along with the following documents

(a) A report from the bankers of the Indian party in a sealed / closed cover.

(b) The latest Annual Accounts, i.e. Balance Sheet and Profit and Loss Account of the Indian party along with the Directors’ Report.

(c) Additional documents as under, if the application is made for partial / full takeover of an existing foreign concern:
   (i) A copy of the certificate of incorporation of the foreign concern;
   (ii) Latest Annual Accounts, i.e. the Balance Sheet and Profit and Loss Account of the foreign concern along with Directors’ Report; and
   (iii) A copy of the share valuation certificate from:
      — a Category I Merchant Banker registered with SEBI, or, an Investment Banker / Merchant Banker registered with the appropriate regulatory authority in the host country, where the investment is more than USD 5 million, and
      — in all other cases, by a Chartered Accountant or a Certified Public Accountant.

(d) A certified copy of the Resolution of the Board of Directors of the Indian party/ies approving the proposed investment.

(e) Where investment is in the financial services sector, a certificate from a Statutory Auditor / Chartered Accountant to the effect that the Indian Party:
   (i) has earned net profits during the preceding three financial years from the financial service activity;
   (ii) is registered with the appropriate regulatory authority in India for conducting the financial services activity;
   (iii) has obtained approval for investment in financial sector activities abroad from regulatory authority concerned in India and abroad; and
   (iv) fulfilled the prudential norms relating to capital adequacy as prescribed by the regulatory authority concerned in India.

9. On submission of ODI to RBI, it will allot a unique identification number to each JVs and WOS abroad which is required to be quoted in all correspondence including additional investment in the existing overseas concern within the specified limits.

10. It has to be ensured to receive share certificate of any other documentary evidence of investment in foreign entity within six months, failing which an application for extension of the same has to be made.

11. Annual Performance Report in the format specified in part III of form ODI, within 3 months of closing the accounts of JVs/WOS as long as it is in existence.

12. It may be noted that an eligible Indian party making investment in a Joint Venture (JV) / Wholly Owned Subsidiary (WOS) outside India is required to route all its transactions relating to the investment through one branch of an AD Category – I
bank designated and all communication from the Indian parties, to the Reserve Bank, relating to the investment outside India should be routed through the same branch of the AD Category – I bank that has been designated by the Indian investor for the investment.

(b) Approval Route

1. Board Resolution is required to be passed under Section 292 of the Companies Act, 1956, specifying the limits for investment by Directors, in respect of out bound investment by the company.

2. Special Resolution has to be passed under Section 372 A of the Companies Act, 1956 for investments in excess of 60% of the paid-up Capital and free reserves or 100% of free reserves whichever is higher and necessary e-form 23 has to be filed with ROC, in case of out bound investment by the company.

3. Part I of form ODI, along with the supporting documents, is required to be submitted after scrutiny and with specific recommendations by the designated AD Category - I bank, to The Chief General Manager, Reserve Bank of India, Foreign Exchange Department, Overseas Investment Division, Amar Bldg. 5th floor, Sir P. M. Road, Fort, Mumbai 400001. In case the proposal is approved, Part I will be returned by the Reserve Bank to the AD Category - I bank. After effecting the remittance, the AD Category – I bank should resubmit the same to the Reserve Bank along with Part II of form ODI along with the following documents.

(a) A report from the bankers of the Indian party in a sealed / closed cover.

(b) The latest Annual Accounts, i.e. Balance Sheet and Profit and Loss Account of the Indian party along with the Directors’ Report.

(c) Additional documents as under, if the application is made for partial / full take over of an existing foreign concern:

(i) A copy of the certificate of incorporation of the foreign concern;

(ii) Latest Annual Accounts, i.e. the Balance Sheet and Profit and Loss Account of the foreign concern along with Directors’ Report; and

(iii) A copy of the share valuation certificate from:

— a Category I Merchant Banker registered with SEBI, or, an Investment Banker /Merchant Banker registered with the appropriate regulatory authority in the host country, where the investment is more than USD 5 million, and

— in all other cases, by a Chartered Accountant or a Certified Public Accountant.

(d) A certified copy of the Resolution of the Board of Directors of the Indian party/ies approving the proposed investment.

(e) Where investment is in the financial services sector, a certificate from a Statutory Auditor / Chartered Accountant to the effect that the Indian Party:

(i) has earned net profits during the preceding three financial years from the financial service activity;

(ii) is registered with the appropriate regulatory authority in India for
conducted the financial services activity;

(iii) has obtained approval for investment in financial sector activities abroad from regulatory authority concerned in India and abroad; and

(iv) fulfilled the prudential norms relating to capital adequacy as prescribed by the regulatory authority concerned in India.

4. On submission of ODI to RBI, it will allot a unique identification number to each JVs and WOS abroad which is required to be quoted in all correspondence including additional investment in the existing overseas concern within the specified limits.

5. It has to be ensured to receive share certificate of any other documentary evidence of investment in foreign entity within six months, failing which an application for extension of the same has to be made.

6. It has to be ensured that repatriation of all the dues takes place within 60 days of its falling due.

7. Annual Performance Report in the format specified in part III of form ODI, within 3 months of closing the accounts of JVs/WOS as long as it is in existence.

8. It may be noted that an eligible Indian party making investment in a Joint Venture (JV) / Wholly Owned Subsidiary (WOS) outside India is required to route all its transactions relating to the investment through one branch of an AD Category – I bank designated and all communication from the Indian parties, to the Reserve Bank, relating to the investment outside India should be routed through the same branch of the AD Category – I bank that has been designated by the Indian investor for the investment.

XII. IMPORTANT CLAUSES IN INTERNATIONAL JOINT VENTURES

A well drafted joint venture agreement should provide a comprehensive road map on the rights and obligations of parties to the agreement and minimizes disputes and complications. Though, the clauses of joint venture agreements cannot be tailor made before signing a joint venture agreement, clauses relating to the following may be addressed.

1. Objectivity
2. Terms and Tenure of the agreement
3. Proportion of holding
4. Managerial control
5. Appointment of Board Members
6. Restriction on sale
7. Arbitration
8. Governing Law
9. Force Majeure Clause
10. Right of first refusal
11. Representation and warranties
12. Clauses relating to patent and IPR issues.
13. Legal compliance
14. Time limits
15. Change of location
16. Change of control
17. Foreign Trade Rights
18. Indemnity Clause
19. Prohibition on assignment
20. Limitation of Liability
21. Confidentiality
22. Severability
23. Termination

CONCLUSION

Setting up of Wholly owned Subsidiaries abroad act as an excellent concourse for facilitating international co-operation and accelerating trade and business. Wholly owned subsidiaries are the need of the hour with this realization.

Setting up of joint ventures abroad is an important avenue of promoting global business by Indian Entrepreneurs in terms of foreign exchange earnings like dividend royalty, technical knowhow fee etc. They are also a major source of increased exports.

**LESSON ROUND-UP**

- Investment in foreign securities is a permissible capital account transaction under schedule I of Foreign Exchange Management (Permissible Capital Account Transactions) Regulations, 2000.
- Setting up of WOS and Joint Ventures requires compliance with various laws in India and the laws and regulations of host country. In India, it is mainly regulated by Foreign Exchange Management (Transfer or Issue of Any Foreign Security) Regulations, 2004 and amendments there on in addition to Companies Act, 1956, FEMA, 1999 and other relevant Acts.
- Indian parties are prohibited from making direct investment in a foreign entity engaged in real estate/banking business.
- According to Regulation 6 of Foreign Exchange Management (Transfer or issue of any Foreign Security) Regulations, 2000, an Indian party is permitted to make investment in overseas Joint Ventures (JV) / Wholly Owned Subsidiaries (WOS), not exceeding 400 per cent of its net worth as on the date of the last audited balance sheet.
- Investments in unincorporated entities overseas in the oil sector (i.e. for exploration and drilling for oil and natural gas, etc.) by Navaratna PSUs, ONGC Videsh Ltd. (OVL) and Oil India Ltd. (OIL) may be permitted by AD Category-I banks, without any limit, provided such investments are approved by the competent authority.
- All applications of Direct Investment outside India which are not qualifying for Automatic route as mentioned in the above mentioned paragraphs are required to obtain prior approval from Reserve Bank of India.
• Indian parties are permitted to capitalise the payments due from the foreign entity towards exports, fees, royalties or any other dues from the foreign entity for supply of technical knowhow, consultancy, managerial and other services within the ceilings applicable.

• A well drafted joint venture agreement should provide a comprehensive road map on the rights and obligations of parties to the agreement and minimizes disputes and complications.

SELF TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation)

1. What are the eligibility criteria for setting up Wholly Owned Subsidiary abroad?

2. Elaborate the procedural requirements of reporting system to RBI in respect of outbound investment under automatic and approval route?

3. What are the important clauses to be covered in the Joint venture agreements?

4. Draft a check list for incorporating a Wholly Owned Subsidiary abroad?
STUDY XI
LEGAL DUE DILIGENCE

LEARNING OBJECTIVES
The objective of this study lesson is to enable the students to understand
- The concept, scope, objectives and process of legal due diligence
- General aspects to be looked during legal due diligence process
- Possible hurdles in legal due diligence
- Role of Company Secretaries in legal due diligence

I. INTRODUCTION

A legal due diligence is scrutiny of all, or specific parts, of the legal affairs of the
target company depending on the purpose of legal due diligence which may be
mergers, acquisition or any major investment decision, with a view of uncovering any
legal risks and provide the buyer with an extensive insight into the company’s legal
matters. It also improves the buyer’s bargaining position and ensures that necessary
precautions are taken in relation to the transaction proposed.

Due diligence is an art that requires expertise in asking gathering and reporting of
sensitive information. It involves collecting information about a corporate or other
company which involves complete details about the products, marketing, financial
status, legal issues, assets/liabilities, etc.

Legal due diligence is a precautionary operation through which one can know the
strengths and weaknesses of the company through the maximum possible
information available. This process reduces future problems and ensures safety.

II. OBJECTIVES OF LEGAL DUE DILIGENCE

The objectives of a legal due diligence exercise may vary from case to case. However some of the common objectives in most of the cases would be as follows:

1. Gathering of information from the target company.
2. Uncovering of the risks of target company through a SWOT analysis.
3. Improving the bargaining position.
4. Cost benefit analysis.
5. Effect of risk and liability on the cost of the transaction.
6. Mapping of compliance requirements of the target company and the actual
   status.

III. SCOPE OF LEGAL DUE DILIGENCE

The scope of due diligence depends on the purpose and objectives of due
diligence and may vary from case to case. The scope of due diligence by a large
institutional investor will vary from the scope of due diligence by the company which
proposes to acquire a target company. Thus it is not possible to define the scope of
due diligence specifically. However, certain mandatory issues that should be covered
in any type of legal due diligence are as follows

1. **Regulatory compliance**
   
   It would include compliance requirements of the company under various
   applicable laws such as Companies Act, Income Tax Act, SEBI Act rules and
   regulations, employee related laws, other business related laws such as
   pollution control laws, patent laws, applicable laws in the country where the
   target company is situated.

2. **Contractual compliance**
   
   It would include the compliance by the company under various material
   contracts by the company with suppliers, customers, employees etc. and to
   verify whether the company has complied with the terms and conditions of
   different contracts.

3. **Compliance under intra-corporate aspects**
   
   It would include the compliance by the company under the intra company
   documents such as Memorandum and Articles of Association, Corporate
   policies, procedures, code of conduct etc.

4. **Financial aspects**
   
   It includes thorough reading of the balance sheet to identify the financial
   obligations of the company, penalties paid for violations of laws in the past
   etc.

5. **Non financial aspects**
   
   It includes aspects such as reputation and goodwill of the company.

6. **Cultural aspects**
   
   Especially in case of cross border transactions, compatibility and
   adaptability of corporate cultures are to be analysed to eliminate the
   problems that may arise out of cultural differences.

The following are the various important aspects covered as scope of due
diligence in general. However, the list provided herein is not an exhaustive list and
the scope would vary according to the nature of business decision.

**Under Companies Act**

- Compliance with provision of Articles of Association
- Related parties transaction
- Appointment of and remuneration to Directors
- Contracts with director
- Loans to Director
- Borrowings by the Company and securities covered
- Matters such as disclosure, prospectus, minimum subscription compliance
  with listing agreement etc. in case of listed company.
— Fixed deposits accepted and its repayments
— Distribution of dividend
— Maintenance of statutory registers, minutes books etc.
— Filing of necessary returns

Under Tax Laws
— Status of tax assessments
— Identification of potential tax liabilities
— Pending notices and demands
— Impact of business agreements on potential tax demands
— Aspects relating to double-taxation.

Under other business laws
— Registrations and approvals from various authorities and risks on non-compliance
— Compliance under pollution control laws
— IPR related matters
— Issues relating to immovable properties, title deeds etc.
— Compliance under FEMA, insurance laws etc.

The investigation or inspection also would cover aspects such as Compliance with local laws, assessment of feasibility of pursuing litigation, reputation and goodwill of the organization, cross-border and cultural issues, employee litigation etc.

IV. NEED OF LEGAL DUE DILIGENCE

Legal Due Diligence provides complete picture of a company through a methodical investigative process. Due Diligence investigations are good at finding liabilities in a company and to uncover the hidden risks. These investigations can help to negotiate a lower price in a business transaction negotiation.

Legal Due Diligence is an art of managing a risk of undertaking a major business transaction. It involves maintaining a methodical system for organizing and analyzing the documents, data, and information provided by the information provider, and then quantitatively assessing the risks associated with any issues or problems discovered during the process. Only a careful and thorough Legal Due Diligence process will help to avoid legal difficulties, unintended transfer of legal property and other drawbacks.

Legal Due Diligence investigations allow getting the current information that is needed to make good business and financial decisions. These investigations help to avoid costly mistakes and can also help to avoid lawsuits caused by a bad business partnership. Investigations such as these can also be crucial in negotiations – by helping cut through business claims to the actual facts about a corporation, they help to get the proof needed to negotiate better terms.
The need for legal due diligence may occur in the following occasions

- Mergers/Acquisitions
- Corporate Restructuring
- Corporate Governance related matters
- IPOs/FPOs
- Private Equity
- General Compliance requirement.
- Commercial agreements
- Leveraged buy-outs
- Joint Ventures etc

V. LEGAL DUE DILIGENCE PROCESS

There is no definitive process of a legal due diligence. The investigative aspects as well as Legal Due Diligence process varies depending upon the scope of work dictated by the client, the focus, special areas of weakness, the type of business, etc. In general, the following process involved in legal due diligence.

- Entering of Memorandum of Understanding between the transacting parties along with confidentiality agreement
- Determination of scope of Legal Due Diligence
- Calculation of time frame
- Drafting of various questionnaire and checklists
- Obtaining of access to records and data room agreement
- Interaction with management and key managerial persons with the questionaires and checklists and for other material information
- Interaction with regulatory authorities for independent check
- Checking of regulatory and contractual compliance
- Analysis of financial and non financial information
- Collation with financial due diligence for confirmation of representations, warranties and liabilities
- Investigation of material issues
- Drafting of preliminary report
- Discussions with the management of the target company
- Finalisation of the Report
- Determination of strategy

VI. GENERAL DOCUMENTS/ASPECTS TO BE COVERED

The following aspects would give a rough figure on the aspects/documents to be
looked into in the process of legal due diligence. However, this is not an exhaustive list.

1. Organizational and internal Aspects
   — Memorandum and Articles of Association of the Company
   — Minutes of all meetings
   — Organisational chart
   — Statutory Registers
   — Returns filed with Ministry of Corporate Affairs and other regulatory authorities.
   — Search/status report if any.
   — Details of branches and subsidiaries
   — Registrations documents under various laws
   — Documents/reports filed with stock exchanges on shareholding pattern and other material information.

2. Financial Aspects
   — Financial Statements for the last five years
   — Auditors Qualifications if any
   — Recent unaudited financial statements
   — Details of various financial reports published under listed agreement
   — Capital Budgets and projections
   — Details of fixed and variable expenses
   — Internal Audit Report if any
   — Strategic plans
   — Details of internal control procedures.
   — Unrecorded liabilities
   — Commitments, contingencies
   — Accounting policies
   — Management, BOD, control environment, Corp Governance etc
   — Relationship between profit and operating cash flows
   — Reliance on debt funds and usage of debt
   — Debt repayment and potential debt trap
   — Working capital lock up

3. IPR/Patent/R&D Details
   — Schedule of trade marks/copyrights
— Details of Indian and international patents with the company
— Details of pending patent applications
— A schedule and copies of all consulting agreements, agreements regarding inventions, licenses, or assignments of intellectual property to or from the Company
— Details of threatened claims if any etc.

4. HR Aspects
— List of employees, their positions and salaries
— Details of options given/vested under ESOP scheme
— Bio-data of key managerial personnel
— Employee litigations
— Employee harassment reports if any.
— Cultural issues in case of cross border transactions.

5. Environmental aspects
— Environmental audits reports if any
— Details of environmental permits and licenses
— Hazardous substances used in the Company's operations
— Copies of all correspondence with environment authorities
— Litigation or investigations if any on environmental issues
— Contingent environmental liabilities or continuing indemnification obligations if any

6. Material Contracts
— A schedule of all subsidiary, partnership, or joint venture relationships and obligations, with copies of all related agreements
— Copies of all contracts between the Company and employees, shareholders and other affiliates
— Loan agreements, letter of credit, or promissory notes etc
— Security agreements, mortgages etc to which the Company is a party
— Any distribution agreements, sales representative agreements, marketing agreements etc.
— All nondisclosure or non competition agreements
— Other material contracts

7. Other aspects
— Copies of any governmental licenses, permits, or consents
— Any correspondence or documents relating to any proceedings of any regulatory agency
— A list of all existing products or services and products or services under development
— Company’s purchase policy/credit policy
— Details of largest customers
— Details of company’s competitors
— Press releases relating to the Company.

VII. POSSIBLE HURDLES IN CARRYING OUT A LEGAL DUE DILIGENCE AND REMEDIAL ACTIONS

1. Non availability of information:
   In many occasions, when a person carries out due diligence, the required information may not be available or insufficient to derive a complete picture.

2. Unwillingness of target company’s personnel in providing the complete information:
   Non-co-operation of target company’s personnel may also prove to be a major hurdle during due diligence process. Sometimes, the available information would be pretended as not available.

3. Providing of incorrect information:
   Providing of incorrect information by the target personal also acts as a major hurdle in the due diligence process.

4. Complex tax policies and hidden liabilities:
   Complex tax policies & structures may create a number of hidden tax liabilities, which may not be easy to track.

5. Multiple Regulations and its applicability:
   Owing to the new and emerging legislations, it is difficult to interpret whether a specific legislation is applicable for business and getting legal opinion on the same would prove to be very costly.

6. Process in providing data:
   Multiple Layers of review and scrutiny before data is provided for due diligence also hinders and delays the due diligence process.

7. Absence of proper MIS:
   Due diligence process would become difficult if there is no proper MIS in the company.

Actions to break hurdles in due diligence

The following actions may break the afore said hurdles
— Focus follow up questions.
— Ask several people the same questions and utilise appropriate professional skepticism.
— Polite persistence may help to overcome this attitude.
— Independent check with regulatory authorities.

Considering this hurdles, it is advisable to insert the necessary disclaimer clauses in the due diligence report.

VIII. ROLE OF COMPANY SECRETARIES IN LEGAL DUE DILIGENCE

Company Secretary is a competent professional who comes in existence after exhaustive exposure provided by the Institute through compulsory coaching,
examinations, rigorous training and continuing education programmes. The course curriculum includes papers on subjects such as Financial Management, Financial Accounting, Company Accounts, Cost and Management Accounting, Financial Treasury and Forex Management, Security Laws and an exclusive paper on ‘Due Diligence and Corporate Compliance Management’. Company Secretary, thus, has vast theoretical knowledge base and practical experience and exposure in various laws and financial aspects. As a Compliance Management specialist, a company secretary is competent to discharge the Legal Due diligence process efficiently.

Company Secretary while carrying out due diligence has to maintain confidentiality. Certain activities conducted during due diligence may breach confidentiality that a transaction is being contemplated. Especially while interacting with external persons such as customers, suppliers, it is better to contact them under the disguise of being prospective supplier/customer, which will help in maintaining confidentiality.

<table>
<thead>
<tr>
<th>LESSON ROUND-UP</th>
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<tbody>
<tr>
<td>• A legal due diligence is scrutiny of all, or specific parts, of the legal affairs of the target company depending on the purpose of legal due diligence which may be mergers, acquisition or any major investment decision, with a view of uncovering any legal risks and provide the buyer with an extensive insight into the company’s legal matters.</td>
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<td>• Legal Due Diligence is an art of managing a risk of undertaking a major business transaction.</td>
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<td>• The documents that is to be checked during legal due diligence may be financial information, statutory information, organizational matters, employee matters etc.</td>
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<tr>
<td>• The process of legal due diligence involves various steps such as entering of MOU, preparations of questionnaires and checklists, interview with target company’s personal, interaction with regulatory authorities, preparation and discussion of preliminary report, finalization of report and arriving of decision.</td>
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<td>• The legal due diligence covers various laws such as Companies, Act, Income Tax Act, other business laws etc.</td>
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<td>1. What do you mean by legal due diligence and why does a person need to carry out legal due diligence.</td>
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<tr>
<td>2. Draft a legal due diligence programme for a corporate acquisition.</td>
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<tr>
<td>3. What are the process involved in legal due diligence in general?</td>
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<tr>
<td>4. What are the possible hurdles that may occur during legal due diligence process.</td>
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LEARNING OBJECTIVES

The objective of this study lesson is to enable the students to understand
- The concept of compliance management
- Scope, significance and need for compliance management
- Compliance Management process
- Systems approach to compliance management
- Compliance in letter and spirit

I. INTRODUCTION

A compliance management system is the method by which corporate manage the entire compliance process. It includes the compliance program, compliance audit, compliance report etc. and in other words it is called compliance solution.

The compliance program consists of the policies and procedures which guide in adherence of laws and regulations. The compliance audit is independent testing of level of compliance with various laws and regulations applicable.

Compliance with law and regulation must be managed as an integral part of any corporate strategy. The board of directors and management must recognize the scope and implications of laws and regulations that apply to the company. They must establish a compliance management system as a supporting system of risk management system as it reduces compliance risk to a great extent. To ensure an effective approach to compliance, the participation of senior management in the development and maintenance of a compliance program is necessary. They should review the effectiveness of its compliance management system at periodic intervals, so as to ensure that it remains updated and relevant in terms of modifications/changes in regulatory regime including acts, rules, regulations etc. and business environment.

Corporate compliance management involves a full process of research and analysis as well as investigation and evaluation. Such an exercise is undertaken in order to determine the potential issues and get a realistic view about how the entity is performing and how it is likely to perform in the future. Company Secretaries with core competence in compliance and corporate governance play a crucial role in the corporate compliance management

II. NEED FOR COMPLIANCE

Corporate accountability is on everyone’s mind today. Business executive face significant pressure to comply with a steady stream of complex regulations. Many companies are adopting comprehensive compliance plans to address emerging regulatory paradigm and those that fail to address the new regulations risk losing
business, paying hefty fines or incurring punitive restrictions on their operations.

As the organizations face mounting pressures that are driving them towards a structured approach to enterprise-wise compliance management, the key drivers of compliance management encompass, the complexity of today’s business, dependency on IT and hitech processes, growth in business partner relationships. Increased liability and regulatory oversight has amplified risk to a point where it demands continuous evaluation of compliance management systems. Furthermore, the multiplication of compliance requirements that organizations face increases the risk of non-compliance, which may have potential civil and criminal penalties.

This focused attention on compliances with spirit and details of laws casts upon Company Secretaries an onerous responsibility to guide the corporates adapting with compliance regimes, so as to ensure extended protection to investors, shareholders and other stakeholders. They have to advise companies in totality to provide full, timely and intelligible information. To enable companies to put in place an effective Compliance Management System, company secretaries should ensure that companies:

— adhere to necessary industry and government regulations,
— Change business processes according to legislative change,
— Realign resources to meet compliance deadlines,
— React quickly and cost-effectively if regulations change.

The risks of non-compliance of the law are many:
1. Cessation of business activities
2. Civil action by the authorities
3. Punitive action resulting in fines against the company/officials
4. Imprisonment of the errant officials
5. Public embarrassment
6. Damage to the reputation of the company and its employees
7. Plummeting stock price and threat of de-listing of shares (in case of listed companies)
8. Attachment of bank accounts.

III. SIGNIFICANCE OF CORPORATE COMPLIANCE MANAGEMENT

1. Better compliance of the law
2. Real time status of legal/statutory compliances
3. Safety valve against unintended non compliances/prosecutions, etc.
4. Real time status on the progress of pending litigation before the judicial/quasi-judicial fora
5. Cost savings by avoiding penalties/fines and minimizing litigation
6. Better brand image and positioning of the company in the market
7. Enhanced credibility/creditworthiness that only a law abiding company can command

8. Goodwill among the shareholders, investors, and stakeholders.

9. Recognition as Good corporate citizen.

Compliance with the requirements of law through a compliance management programme can produce positive results at several levels:

— Companies that go the extra mile with their compliance programs lay the foundation for the control environment.

— Companies with effective compliance management programme are more likely to avoid stiff personal penalties, both monetary and imprisonment.

— Companies that embed positive ethics and effective compliance management programme deep within their culture often enjoy healthy returns through employee and customer loyalty and public respect for their brand, both of which can translate into stronger market capitalization and shareholder returns.

Clearly, the benefits of implementing and maintaining an effective ethics and compliance program far outweigh its costs. Not only does the compliance management protect investors wealth but also helps the business in running successfully with any potential risk being addressed in a timely and accurate manner.

Since 1991, in USA, the companies that create, communicate, enforce, and promote effective compliance programs, as defined by the U.S. Federal Sentencing Guidelines for Organizations, have been given favorable treatment by the Department of Justice, even when misconduct by employees in their organizations has been proven. The resultant savings, in terms of mitigated fines, has totalled hundreds of millions of dollars.

IV. ELEMENTS OF AN EFFECTIVE COMPLIANCE PROGRAM

The U.S. Federal Sentencing Guidelines for Organizations provide a clear framework for corporate compliance program. According to these Guidelines, the key elements of a program should include:

— Standards and procedures to prevent criminal conduct.

— Oversight by high-level person(s) (e.g., Chief Compliance Officer).

— Care in delegation of substantial discretionary authority to individuals (e.g., background checks).

— Effective communication of standards and procedures.

— Reasonable steps to achieve compliance (e.g., reporting systems, help line).

— Consistent enforcement of disciplinary mechanisms.

— Appropriate response after detection of an offence.

The underlying process for compliance management is nearly the same for every regulation:
— Use of assessments, audits, inspections or incoming complaints to identify non-conformance.

— Identification of the non-conformance which needs remedial action.

— Providing a mechanism for defining, tracking and implementing corrective actions to address non-conformance.

— Use of change control techniques such as document management or training to ensure that the corrective action is implemented.

— Providing visibility into the entire process through reporting and dashboards.

V. PROCESS OF CORPORATE COMPLIANCE MANAGEMENT AND REPORTING

Installing proper compliance process is a must for the success of compliance programme. Systematic approach helps in chalking out a plan of action in right direction. Installing a process presupposes planning for the activity, identification of desired objective and resources, detailed plan of action with provision for eventualities and continuous monitoring and corrective measures.

It is desirable that the compliance management process is so designed that it is able to generate a complete MIS Report for secretarial and legal data providing the key information including company details, key dates, brief information about company’s business, certifications obtained, addresses of office locations, details of Board of Directors, shareholding pattern, key registration nos. such as company registration no., scrip code, ISIN code etc., contact details of agencies such as auditors, consultant, banker, government agencies, printers, R&T agents etc. Purely for a legal function database of immovable properties, on-going litigations, compliance reports, list of power of attorneys issued etc. prove immensely useful and provide timely information, to take necessary action to correct non-compliance, if any.

It is essential to segregate roles and responsibilities within the function to ensure proper distribution of work, rotation of responsibilities where possible, avoid confusion and set focus for each person within the function.

Considering the multiplicity of laws that are applicable to companies in India, a systematic approach to corporate compliance management is worth doing an exercise to go through a list of laws and identifying those relevant to the industry and business to which the company belongs and categorizing them in future to focus on critical compliances. Critical compliance means the severity of compliance and its impact on business, while it is true that all laws are of equal importance and should be complied with in letter and spirit.

VI. SCOPE OF CORPORATE COMPLIANCE MANAGEMENT

Corporate compliance management should broadly include compliance of:

— Corporate Laws
— Securities Laws
— Commercial Laws including Intellectual Property Laws
— Labour Laws
— Tax Laws
— Pollution Control Laws
— Industry Specified laws
— All other Laws affecting the company concerned depending upon the type of industry/activity.

The details of the above mentioned legislations are given below.

(a) Corporate & Economic Laws

Corporate laws are core competence areas of a Company Secretary and corporate compliance management broadly requires complete compliance of these laws. Some of the important corporate laws are given below in brief:

— Companies Act, 1956 and the various Rules and Regulations framed there under, MCA-21 requirements and procedures.
— Secretarial Standards/Accounting Standards/Cost Accounting Standards issued by ICSI/ICAI/ICWAI, respectively.
— Foreign Exchange Management Act, 1999 and the various Notifications, Rules and Regulations framed there under.
— Competition Law.
— Special Economic Zones Act, 2005.

(b) Securities Laws

— SEBI Act, 1992
— Securities (Contracts) Regulation Act, 1956 and rules made thereunder
— Various rules, regulations guidelines and circulars issued by SEBI
— Provisions of Listing Agreement
— Sarbanes-Oxley Act, 2002 and other legislations etc, wherever applicable.
— Depositories Act, 1996

(c) Commercial Laws

— Indian Contract Act, 1872
— Transfer of Property Act, 1882
— Arbitration and Conciliation Act, 1996
— Negotiable Instruments Act, 1881
— Sale of Goods Act, 1930

(d) Fiscal Laws
— Income Tax Act, 1961
— Central Excise Act, 1944
— Customs Act, 1962
— Wealth Tax Act, 1957
— Central Sales Tax/State Sales Tax/VAT
— Service Tax.

(e) Labour Laws
— Minimum Wages Act, 1948
— Payment of Bonus Act, 1965
— Payment of Gratuity Act, 1972
— Employees’ Provident Funds and (Misc. Provisions) Act, 1952;
— Employees’ State Insurance Act, 1948;
— Factories Act, 1948;
— Workmen’s Compensation Act, 1923;
— Maternity Benefit Act, 1961;
— Industrial Dispute Act, 1947; and

(f) Pollution/Environment related Laws
— Air (Prevention and Control of Pollution) Act, 1981
— Water (Prevention and Control of Pollution) Act, 1974
— Water (Prevention and Control of Pollution) Cess Act, 1974
— Environment Protection Act, 1986

(g) Industry Specific Laws
Legislations applicable to specific categories of industries – electricity, power generation and transmission, insurance, banking, chit funds, etc.

(h) Local Laws
These would include Stamp Act, Registration Act, municipal and civic administration laws, shops and establishments, etc.

Individual companies may suitably add or delete to/from the above list as required.
Role of Information Technology

A critical component of an effective compliance program is the ability to monitor and audit compliance in a “real time manner.” Yet, as companies cross geographical and industry boundaries, it is becoming harder to perform this role in the traditional manner. As a result, companies are increasingly seeking technology solutions.

VII. THE SYSTEMS APPROACH

A well-designed compliance management programme has abilities to perform the following key functions across the enterprise:

— **Compliance Dashboard:** The compliance programme must provide a single enterprise-wide dashboard for all users to track and trend compliance events. All compliance events should be easily viewed interactively through the enterprise compliance dashboard. External auditors, internal auditors, compliance officers can use the dashboards to make decisions on the compliance status of the organization.

— **Policy and Procedure Management:** A well-designed document management system forms the basis of managing the entire lifecycle of policies and procedures within an enterprise. Ensuring that these policies and procedures are in conformity with the ever-changing rules and regulations is a critical requirement. The creation, review, approval and release process of the policy documents and SOPs (Standard Operating Procedures) should be driven by collaborative tools that provide core document management functionality.

— **Event Management:** The compliance management system must have ability to capture and track events, cases and incidents across the extended enterprise. Compliance officers, call center personnel, IT departments, QA personnel, ethics hotline should be able to log in any adverse event across the enterprise, upon which the necessary corrective and preventive actions are initiated.

— **Rules and Regulations:** A well-designed compliance management solution must offer capabilities for organization to continuously stay in sync with changing rules and regulations. As soon as there are regulatory changes, the various departments should be notified proactively through “email based” collaboration. This process critically enables the organization to dynamically change their policies and procedures in adherence to the rules and regulations. While tracking a single regulation may be manually feasible, it becomes an error-prone task to track all local, state, and central regulations including those taking place across the globe. A well-designed Compliance management programme offers up-to-date regulatory alerts across the enterprise.

— **Audit Management:** Audits have now become part of the enterprise core infrastructure. Internal audits, financial audits, external audits, vendor audits must be facilitated through a real-time system. Audits are no more an annual activity and corporations offer appropriate audit capabilities. Appropriate evidence of internal audits becomes critical in defending compliance to
— **Quality Management**: Most organizations have internal operational, plant-level or departmental quality initiatives to industry mandates like Six-sigma or ISO 9000. A well-designed compliance management program incorporates and supports ongoing quality initiatives. Most quality practitioners agree that compliance and quality are two sides of the same coin. Therefore, it is critical to ensure that compliance management solution offers support for enterprise-wide quality initiatives.

— **Training Management**: Most compliance programs often require evidence of employee training. Regulations like Clause 49 of Listing Agreement and Sarbanes-Oxley Act, stress on employee training. In USA, lack of documented training can lead to fines and penalties. Often the compliance office has to work closely with the HR organization to facilitate employee training. Well-designed compliance program requires a well-integrated approach to training management.

— **Compliance Task Management**: Organizations must plan, manage and report status of all compliance related activities from a centralized solution. Automated updates from the various compliance modules should provide for up-to-the-minute status reporting that could be viewed by the Board, corporate compliance officer, entity compliance coordinators, quality offices and others as designated.

**Compliance solutions**

In this age of information technology and outsourcing, where corporate solutions are available at every step and in respect of every matter, there are several companies offering ‘compliance solutions’.

**Approach to Compliance Solutions**

Compliance solution providers adopt following approaches for creating or enhancing an ethics and compliance program for companies—

**Risk/Cultural Assessment**: Through employee surveys, interviews, and document reviews, a company’s culture of ethics and compliance at all levels of the organization is validated. Our Reports and recommendations with detail observations identify gaps between company’s current practices and benchmarks with international practices.

**Program Design/Update**: In this phase, compliance solution providers help company in creating guideline documents that outline the reporting structure, communications methods, and other key components of the code of ethics and compliance program. This encompasses all aspects of the program, from grass roots policies to structuring board committees that oversee the program; from establishing the mandatory anonymous complaint reporting mechanism—i.e., compliance and ethics help line or whistleblower hot line—to spelling out the specifics of the code of ethics in a way that is easily understood by everyone at all levels of organization.

**Policies and Procedures**: In this phase compliance solution providers help company to develop or enhance the detailed policies of the program, including issues of financial reporting, antitrust, conflicts of interest, gifts and entertainment, records
accuracy and retention, employment, the environment, global business, fraud, political activities, securities, and sexual harassment, among others.

**Communication, Training, and Implementation:** Even the best policies and procedures are useless if they are not institutionalized—they must become part of the fabric of the organization. Compliance solution providers help company to clearly articulate, communicate, and reinforce not only the specifics of the program, but also the philosophy behind it, and the day-to-day realities of it. In this way, key stakeholders and other personnel are more likely to embrace the program and incorporate it into their attitudes and behaviours.

**Ongoing self-Assessment, Monitoring, and Reporting:** The true test of a company’s ethics and compliance program comes over time. How do one know in one year or five that both the intent and letter of the law are still being observed throughout organization? How does the program—and the organization—adapt to changing legislation and business conditions? As the organization evolves—for example, through mergers and acquisitions—will the program remain relevant? The cultural assessment, mechanisms, and processes put in place including employee surveys, internal controls, and monitoring and auditing programs, help organisations achieve sustained success.

**VIII. COMPLIANCE WITH SPIRIT OF LAW (ETHICS)**

In the context of corporate governance, compliance means obeying the law. Ethics is the intent to observe the spirit of law—in other words, it is the expressed intent to do what is right. In the wake of recent corporate scandals, a program that strongly emphasizes both ethics and compliance is good business.

The Sarbanes-Oxley Act of 2002, along with related mandates by the Securities and Exchange Commission and new listing rules instituted by the major stock exchanges including India, raise the ante for ethical behavior and effective corporate compliance programs. Public companies and their senior executives and board members may be held accountable—personally accountable in the case of the executives and board members—not only for the financial reporting provisions of the legislations, but also for the aspects pertaining to ethics and corporate compliance. Companies and their leadership that adhere both to the letter and the spirit of the law can achieve substantial benefits.

An ethical compliance management programme ensures that the mechanisms are in place to provide early warning of deviations from guidelines and regulations. It is essential to create or expand a culture of trust, enthusiasm, and integrity - critical attributes that can produce measurable results in terms of productivity, employee satisfaction, customer satisfaction, and, ultimately, brand equity.

**IX. ROLE OF COMPANY SECRETARIES**

Corporate Compliance Management can add substantial business value only if compliance is done with due diligence. A Company Secretary is the ‘Compliance Manager’ of the company. It is he who ensures that the company is in total compliance with all regulatory provisions. Corporate disclosures, which play a vital role in enhancing corporate valuation, is the forte of a Company Secretary. These disclosures can be classified into statutory disclosures, non-statutory disclosures,
specifies disclosures and continuous disclosures. Clause 49 of Listing Agreement spells out elaborately on various aspects of disclosures which are to be made by the company such as contingent liabilities, related party transactions, proceeds from initial public offerings, remuneration of directors and various details giving the threats, risks and opportunities under management discussion and analysis in the corporate governance report which is published in the annual accounts duly certified by the professional like company secretaries. A Company Secretary has to ensure that these disclosures are made to shareholders and other stakeholders in true letter and spirit.

In nutshell, the Company Secretary is the professional who guides the Board and the company in all matters, renders advice in terms of compliance and ensures that the Board procedures are duly followed, best global practices are brought in and the organisation is taken forward towards good corporate citizenship.

Illustration

An illustrative study on compliance management programme with hypothetical figures, is given below for better understanding.

Compliance with the regulatory acts not only protect investors wealth but also helps the business in running successfully with any potential risk being addressed in a timely and accurate manner. A well drafted compliance management programme will function as a compliance solution that monitors the effectiveness of various controls applied to mitigate risks.

For example XYZ Ltd., a listed broking company may have compliance management programme covering the following aspects. It may be noted that this may not be a very comprehensive one.

Compliance Management Programme for XYZ Ltd.

I. Background of the company

XYZ Ltd. (herein after called ‘the company’) is a leading broking firm incorporated on 10th February, 1991, having its registered and corporate office located at Delhi and having 120 employees. The company was promoted by Mr. X, Mr. Y and Mrs. Z who are having experience in financial services sector for more than 25 years, 19 years, and 20 years respectively. The networth of the company as on March 31, 2008 was Rs……………. crores and the market capitalization as on September 03, 2008 was Rs……………. crores.

The company is handling sizeable portion of equities and derivatives being traded on NSE and BSE. The major activities and offerings of the company today are Equity Broking and Depository Participant Services. The company is a member of the National Stock Exchange of India, Bombay Stock Exchange of India and is a Depository Participant with National Securities Depository Limited and Central Depository Services (I) Limited. The company is a listed company with BSE and NSE. The company has also issued shares under FDI scheme.

II. Identification of applicable laws

The role of information technology in identifying the applicable laws is really vital.
The company can identify the applicable laws just by click of a button through software, which has to be updated from time to time. It may be possible that some of the legislations might be missed out while listing the applicable laws manually and thus Compliance management through system would help in

(i) Identifying risk attributes (i.e. identifying the applicable laws)
(ii) Application of control to mitigate the risk (control check list under various legislations (both time based and event based)
(iii) Generation of reports for identifying the non compliances
(iv) Reminder before the due date for compliance
(v) Having internal control on compliance.

In respect of the said XYZ limited, the following sample check list on applicable laws would give an idea on the same.

(It may be noted that the laws listed out here is general about drafting a compliance programme and may not be too comprehensive.)

(a) General applicability

(i) The Companies Act, 1956
(ii) Income Tax Act, 1961
(iii) Contract Act, 1872
(iv) Stamp Act
(v) Negotiable Instruments Act, 1881

(b) Company-specific applicability (i.e. a listed broking company)

(i) SEBI Act, 1992
(ii) Securities Contracts (Regulation) Act, 1956
(iii) Securities Contracts (Regulation) Rules, 1957
(iv) Depositories Act, 1996
(v) Prevention of Money Laundering Act, 2002
(vi) SEBI (Intermediaries) Regulations, 2008
(vii) SEBI (Stock Brokers and Sub-brokers) Regulations, 1992
(viii) SEBI (Depositories and Participants) Regulations, 1996
(ix) BSE/NSE bye laws, rules and regulations
(x) Listing agreement

(c) Labour laws

(i) The Employees Provident Funds and Miscellaneous Provisions Act, 1952
(ii) The Employees State Insurance Act, 1948
(iii) The Maternity Benefit Act, 1961
(iv) The Minimum Wages Act, 1948
(v) The Payment of Bonus Act, 1965
(vi) The Payment of Gratuity Act, 1972
(vii) The Child Labour (Prohibition and Regulation) Act, 1986
(viii) Payment of Wages Act, 1936
(ix) The Workmens Compensation Act, 1923

(d) Applicable State Laws

(e) Transaction based application
   (i) FEMA 1999
   (ii) FDI scheme

   Individual checklists (time based and event based) may be prepared as a control system.

III. Individual responsibilities on compliances to be clearly defined

   Responsibility with respect of compliances has to be clearly defined in the compliance management programme, which will enable the compliance officer to coordinate with the respective officials in respect of deviations if any. For example, person responsible for PF returns from HR department, person responsible for reports to be sent to NSE in respect of terminals etc. may be given clearly.

IV. Evaluation

   Compliance management system should have a proper evaluation methodology through questionnaires to departmental heads etc. at regular intervals.

V. Bridging the gap between compliance in letter and compliance in letter and spirit

   As we discussed compliance has to be carried out in letter and spirit. The compliance management system has to be made in such a manner that the compliance is made in letter and spirit.

VI. Updation

   Updation of compliance management programme is very essential as and when there is any change in any of the applicable law.

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**LESSON ROUND-UP**

- A compliance management system is the method by which corporate manage the entire compliance process. It includes the compliance program, compliance audit, compliance report etc.
- A tool, which helps companies comply with provisions of various governing legislations as well as rules, regulations and guidelines issued thereunder, is a Compliance Solution.
- In the context of corporate governance, ethics is the intent to observe the spirit of law—in other words, it is the expressed intent to do what is right.
- Corporate Compliance Management can add substantial business value only if compliance is done with due diligence.
The Company Secretary is the professional who guides the Board and the company in all matters, renders advice in terms of compliance and ensures that the Board procedures are duly followed, best global practices are brought in and the organisation is taken forward towards good corporate citizenship.

SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. Draft a Compliance Management programme for a Broking company.
2. Describe the scope of compliance management.
3. Explain compliance management process in general.
4. Explain the systems approach to compliance management.
STUDY XIII
SECRETARIAL AUDIT

LEARNING OBJECTIVES
The objective of this study lesson is to enable the students to understand
• Meaning, Need, Objectives, scope and process of secretarial audit
• Format of Secretarial Audit Report
• Checklists under Corporate, Industrial, SEBI, Foreign Exchange laws etc.

INTRODUCTION

Law acts as a means of achieving the planned development of the policies and programmes of a Welfare State. Since a corporation does not act in isolation but within the society itself, its activities have a tremendous bearing on the economic development of the society and its policies and programmes affect the employees, consumers, the exchequer, shareholders, creditors and society at large. It is no longer held to be a valid doctrine that the business enterprise exists solely for profit and for its shareholders and owners. The modern corporation cannot afford to survive and grow merely on the strength of owned funds and has to rely increasingly on funds from public financial institutions and banks and also funds provided by the public (investors). If the corporation fails to take care of the interest of labour, consumers, shareholders, small industries or the national economy as a whole, it cannot be said to have discharged its responsibilities fully and truly as an organ of the society.

Over the last few decades, the running of business has become comparatively intricate as a result of cataclysmic changes in the internal composition of the companies and increase in external pressures on their management. The companies are increasingly coming in close contact with the society and the activities of certain corporations may cause danger to individuals as well as create environmental hazards and economic loss to the community at large.

With the growing complexities of modern business and the ever increasing number of laws to regulate and develop various sectors of the economy, the Board of directors and the company managements have to traverse a wide spectrum of legal and procedural compliances. Companies and the Members of the Board of Directors are required to comply with not only the various provisions of important legislations like the Companies Act, 1956, SEBI Act, 1992, the Foreign Exchange Management Act, 1999, Industries (Development and Regulation) Act, 1951 the Water (Prevention and Control of Pollution) Act, 1974, the Air (Prevention and Control of Pollution) Act, the Environment (Protection) Act, 1986, the Consumer Protection Act, 1986, Direct and Indirect Tax Laws, Labour Laws etc. as amended from time to time but also the Rules, Regulations, Notifications, Clarifications, Guidelines issued from time to time by the Government under these Acts. These laws impose onerous duties on Company Directors and Company Executives. As a consequence of these developments, greater reliance is being placed by all companies - be it a public limited company or a private limited company - on the qualified Company Secretaries.
who can ensure compliance with the Rules, Regulations, Notifications etc. issued under the said Acts.

SECRETARIAL AUDIT

Secretarial Audit comprises of verification by an independent professional of compliance with rules, procedures, maintenance of books, records etc., to monitor compliance by a company with various legal requirements. In other words, Secretarial Audit is a post facto exercise comprising of detailed verification of formalities, procedures, maintenance of documents etc., to ensure that the company has properly complied with various legal requirements.

It is essentially a pre-emptive audit which seeks to monitor and ensure compliance with the requirements of various laws. Just as statutory audit deals with financial audit of companies and cost audit with audit of costing and pricing systems and records, Secretarial Audit is expected to deal with procedural and legal compliances that are expected from a company. Some companies, acknowledging the utility of Secretarial Audit by a company secretary in practice have voluntarily opted to prescribe Secretarial Audit. For the financial institutions/corporations such an audit gives a reassurance in the matter of compliances by the assisted companies, with important corporate laws. Statutorily prescribing Secretarial Audit would result in qualitative improvement in and control by the office of the Registrar of Companies and would also save valuable time and resources of companies.

Clause (c)(v) of Section 2(2) of the Company Secretaries Act, 1980 provides that a member of the Institute in practice can act as or perform services as can be performed by a “Secretarial Auditor” or consultant.

Need for Secretarial Audit

Secretarial Audit not only acts as an effective mechanism to ensure that the legal and procedural requirements are duly complied with but also instills professional discipline in the working of the company besides building up the necessary confidence in the state of affairs of the company.

Several industrial and corporate laws need to be complied with by companies, non-compliance of which attracts prosecution. Secretarial Audit has a capability to provide an in-built mechanism for ensuring corporate compliance generally and will specifically help restore this confidence of investors through greater transparency.

Secretarial Audit extends professional help to the company in carrying out effective compliances and establishment of proper systems with appropriate checks and balances. Secretarial Audit is inherently useful, especially to small and medium sized companies and in particular, to the professional/nominee directors.

It relieves the company and its directors including the nominee directors, from the consequences of unintended non-compliances of the provisions of the Companies Act and other important corporate laws. It further curbs the tendency on the part of the smaller companies to short cut the procedural requirements which is primarily due to ignorance or lack of professional support. Secretarial Audit essentially acts as a pre-emptive check to monitor compliance with requirements of the Companies Act and other important corporate laws. The company secretary, while undertaking secretarial
audit, acts as a friend and guide to the management of companies and educates and, assists them in complying with the various legal and procedural requirements.

Secretarial audit also assists the government in ensuring better compliance of law and reduces litigation.

Further, with the growing reliance of companies on institutional finance/working capital from All-India and State level financial corporations and banks, it has become imperative for such agencies to know that the company has complied with the core legislations. Secretarial audit provides the much needed case due to proper maintenance of statutory records and compliance with the legal and procedural requirements.

Secretarial audit not only ensures that the company has complied with the provisions of various laws but also extends professional help to the company in carrying out effective compliance and establishment of proper systems with appropriate checks and balances.

In order to ensure better self-regulation on the part of companies and due compliance with the provision of law, secretarial audit of those companies which are not subject to the production of compliance certificate, is an imperative necessity.

**Objectives of Secretarial Audit**

Economic, industrial and corporate laws impose numerous obligations for compliance on companies in order to subserve the needs of the public, investors, employees, shareholders and creditors. Introduction of Secretarial Audit will help in ensuring adequate compliance with the provisions of various laws, and by providing effective follow-up by an independent professional. The Secretarial Audit Report highlights that the various provisions under the legislations applicable to the company have been complied with. It vouches that the company and the top management have duly complied with all the requirements of the Acts covered. Such an audit, thus, helps the administering authorities and institutions which have extended financial assistance to the companies.

The whole objective of secretarial audit is not to find fault in the working of companies but to regulate the same. It is possible through pressure of work or over sight or for any other cause that the company concerned has not established compliance with some statutory or contractual requirement. Such non-compliances will come to light if an outside person looks into the same and corrective action can be taken at the earliest to ensure effective compliance with the obligations.

**Benefits of Secretarial Audit**

Secretarial Audit can prove to be an effective and multipurpose mode to assure the regulator, generate and repose confidence amongst the shareholders, creditors and other stakeholders in companies, assure Financial Institutions, including state level Financial Institutions etc. and instill self regulation and professional discipline in companies. Secretarial Audit assists in gauging immediately the level of compliances or non-compliances by the company and prompt corrective measures taken. This would reduce the number of prosecutions by government and consequent litigations; thereby resulting in a healthy and orderly development of the corporate sector.
Benefits to the Government

(a) Ensuring professionalism in management.
(b) Better compliance of laws, rules and regulations etc.
(c) Instilling self-regulation and professional discipline in companies.
(d) Effective regulation of companies.
(e) Considerable reduction in cases of oppression and mismanagement.
(f) Building up of corporate culture.
(g) Healthy and orderly development of the corporate sector.
(h) Timely availability of authentic documents at the office of ROC for public inspection.
(i) Enabling the Government to regulate companies on ‘management by exception’ principle.

Benefits to the Companies

1. Instilling professionalism.
2. Effective control and proper corporate governance.
3. Avoiding disputes and litigation by law enforcing agencies.
4. Improving and strengthening quality and speed of investor services.
5. Nurturing investors and creditors confidence.
6. Ease in raising of finances from Banks and Financial Institutions due to proper maintenance of statutory records.
7. Improving corporate image.

Benefits to FIs/SFCs/SIDCs and other Institutional Investors/Creditors

1. Assurance that the affairs of the assisted company are being conducted as per law;
2. Timely receipt of performance reports leading to better appreciation and evaluation of company performance;
3. Timely creation of security;
4. Availability of documents for inspection at the offices of ROCs;
5. Facilitating timely intervention as and when warranted.

Benefits to Non-Executive/Nominee Directors

1. Relieving the directors from the consequences of unintended non-compliance of law due to ignorance or lack of professional expertise.
2. Strengthening the institution of directors.
3. Encouraging the participation of directors.
4. Encouraging to participate actively and to contribute independently in company’s affairs.

Benefits to shareholders and debenture holders

1. Timely corporate actions with respect to payment of dividend/interest/
redemption/conversion of securities, endorsement of calls, rights, bonus issues etc.

2. Faster registration of securities’ transactions.

3. Assurance as to proper compliance with laws, rules, regulations, etc. and ensures that the owners stake is not being exposed to undue risk.

4. Improved investor confidence.

Cost-Benefit Analysis

When there is a non-compliance, the management, in order to rectify the non-compliance has either to face prosecution and fines or to seek compounding of the offence on payment of compounding fee. If preventive measures are taken by utilizing the services of Company Secretaries in practice, there would not only be, no consequences of non-compliances but also the managements would have more time and resources to concentrate on the business of the company. In the ultimate analysis, the services of Company Secretaries in Practice who are independent professionals, to advise the management on proper procedures and compliance will not only bring about professionalism in the working of the company but also save on a lot of cost and time involved in litigation or compounding besides a minimum standard of good corporate governance.

Scope of Secretarial Audit

Secretarial Audit may, for the present be confined to the following compliances:

(i) Under the Companies Act, 1956

(a) Whether necessary statutory formalities in connection with promotion and incorporation of companies have been complied with.

(b) Whether statutory registers/records etc., as laid down in the Act, have been maintained by the company.

(c) Whether various forms/returns/copies of resolutions, etc. to be filed with the Registrar of Companies and other authorities under the Act, have been filed correctly and promptly.

(d) Whether the appointment of managerial personnel has been properly made.

(e) Whether requisite approvals have been obtained from the authorities for specific proposals.

(f) Whether the terms and conditions of approvals have been followed/satisfied.

(g) Whether the meetings of the board of directors/general body of shareholders have been properly held as per law.

(h) Whether in refusing registration of transfer of shares the provisions of Section 111 of the Act have been complied with.

(i) Whether due disclosures have been made by the company and the company has complied with the requirements in pursuance of the disclosures made by its directors.

(j) Whether the issue of capital and securities is in conformity with the requirements(including any rights/bonus/preferential issue).
(k) Whether the certificates of shares and other securities have been issued and the transfer and transmissions thereof have been registered as per the requirements.

(l) Whether statutory requirements for dematerialisation of shares and other securities have been met properly.

(m) Whether right to dividend, rights shares and bonus shares have been duly held in abeyance pending registration of transfer of shares.

(n) Whether procedure for buy-back of securities has been duly followed.

(o) Whether the borrowings of the company from directors, shareholders, public financial institutions, banks and others have been made in accordance with the requirements of the Companies Act and loans to directors are duly made.

(p) Whether the loans and investments have been made by the company in accordance with the requirements and necessary formalities for inter corporate loans have been complied with.

(q) Whether necessary disclosures and procedural requirements have been met in connection with contracts with or to directors and other interested parties.

(r) Whether particulars of creation, modification and satisfaction of charges conferring security on the company’s property or undertaking have been filed with the Registrar as per the requirements.

(s) Whether the terms and conditions in connection with merger, takeover and amalgamation are complied with and are in accordance with takeover code.

(t) Whether there has been a general compliance with the requirements of the Companies Act, 1956.

(ii) Under the SEBI Act, 1992 and SEBI (DIP) Guidelines, 2000

Whether necessary compliances under SEBI (DIP) Guidelines, 2000 for various issues, various rules, regulations of SEBI have been carried out.

(iii) Under the Monopolies and Restrictive Trade Practice Act, 1969

Whether the terms and conditions of orders passed by the authorities under the MRTP Act have been complied with.

(iv) Under the Foreign Exchange Management Act, 1999

(a) Whether necessary approvals, wherever required have been obtained in connection with in bound and out bound investments.

(b) Whether the procedural formalities have been complied with regard to remittance of royalty/dividend/interest to non-residents.

(c) Whether necessary approvals have been obtained in regard to appointment of foreign nationals.

(d) Whether necessary approvals have been obtained for current account transactions.

(v) Under the Securities Contracts (Regulation) Act, 1956

(a) Whether the company has complied with the terms and conditions stipulated
(b) Whether the company has complied with the guidelines issued by the government, from time to time.

(vi) *Under the Water and Air Pollution Control Laws*

(a) Whether the company has obtained requisite approvals under the Air and Water Pollution Laws.

(b) Whether the directions issued by the pollution control and other authorities under these laws have been complied with.

(c) Whether any accident leading to discharge of pollutants into the atmosphere took place and if so what consequences followed.

(d) Whether any show cause notice/prosecution has been issued against the company for violation of any provisions of the relevant Acts.

(vii) *Under Select Industrial and Labour laws*

(a) Whether the company has obtained necessary approvals and permission for exempting the application of the provisions as may be required under important industrial and labour laws.

(b) Whether the company has maintained proper books and records.

(c) Whether the company has given proper notices/filed proper returns with the various statutory authorities.

(d) Whether any show cause notice/prosecution has been received/launched against the company for violation of any industrial and labour laws.

(viii) *Under Presentation of Money Laundering Act, 2002*

Whether company has reported suspicious cash transactions if any to financial intelligence unit – India.

(ix) *Under the Contractual terms with the financial/industrial development/ investment corporations*

Whether the terms and conditions stipulated in the loan agreement have been complied with.

**SECRETARIAL AUDIT REPORT**

**Meaning and Scope**

Secretarial Audit Report is a report prepared by the secretarial auditor, confirming the maintenance of statutory registers, minutes books, due convening of meetings of the company, approvals required from various authorities under the Companies Act, Monopolies and Restrictive Trade Practices Act, etc. At present, it is optional for a company to arrange for a Secretarial Audit.

For the conduct of secretarial audit members can evolve their own procedure keeping in view the objective of the Audit. The starting point for such an Audit should invariably be:
— Memorandum and Articles of Association,
— the Minutes of the Board Meetings for the past few years (say past three years),
— the Minutes of Annual and Extra-ordinary general meetings held during the last few years (say three years),
— subsisting agreements with financial and other institutions for financial and other assistance,
— Collaboration agreements, if any,
— Statutory Registers maintained by the company,
— Various electronic forms/documents filed with MCA under Section 610B of the Companies Act, 1956,
— Provisions of the Act, rules, regulations, guidelines, administrative instructions framed or issued thereunder as are relevant for the functioning of the company and for carrying on the business.

On a careful examination of the documents and registers mentioned above the Secretarial Auditor can list out the various points to be looked into by him. The Memorandum and Articles of Association will throw light on the business activities that the company concerned could engage in and the procedure for pursuing the same. The Board and General Meetings’ minutes will throw light on the decisions taken by the company in implementation of the business objectives. The agreements with financial institutions and other institutions and the collaboration agreements will throw light on the negative and other covenants agreed to by the company concerned. Having listed out the points, the Secretarial Auditor should find out whether the company has in regard to each point established compliance with the statutory and contractual requirements therefor. To illustrate, if a company in implementation of one of its objects has taken a decision to invest in another company, the following should be examined:

— Whether the investment proposed is authorised by the objects clause of the Memorandum of Association of the company?
— Whether the investment proposed is within the powers of the Board to make with reference to Sections 292 and 372A of the Act?
— If it is beyond the powers of the Board whether the approval of the shareholders therefor has been obtained.
— Whether approval of the financial institutions has been obtained for making the investment?
— Whether the investment has been entered in the Register of investments?

If any of the compliances has not been made this should be clearly brought out in the Secretarial Audit Report. Likewise the secretarial auditor should examine whether all required compliances have been established in regard to various points listed by him.

As per the guidelines evolved by the Institute for engagement of a Secretarial
Auditor, it has been proposed that the Secretarial Auditor shall submit his report to the Board of Directors. The Secretarial Audit Report may also be provided to shareholders as Annexure to the Director’s Report.

Although the concept of and the need for Secretarial Audit has been recognized, the audit is yet to be statutorily prescribed. As a result of continuous dialogue since 1980 with the members on various aspects of practice and the scope for practising members, and based on the information compiled from such interaction, a format of secretarial report has been evolved by the Institute, purely as a guideline for those intending to take up practice as a secretarial auditor. The information contained in the format evolved by the Institute is purely suggestive and recommendatory, intended to serve only as a guideline, where the individual company decides to undertake Secretarial Audit on a voluntary basis.

The suggested format evolved by the Institute is given below:

**FORMAT OF SECRETARIAL AUDIT REPORT**

To

The Board of Directors......... Ltd.

I. Subject to observations made in Annexure A to this Report, I report that under the provisions of the Companies Act, 1956:

(a) the company has/has not properly maintained all the statutory registers, minute books and other relevant records;

(b) all forms, returns, documents and copies of resolutions required to be filed have/have not been duly filed with the prescribed authorities;

(c) requirements as to meetings of shareholders and directors have/have not been complied with;

(d) in relation to all managerial appointments, the requirements of the Act have been complied with;

(e) approvals* of shareholders, Board of Directors, and Government authorities, wherever required, have been obtained, and

(f) the company has/has not refused any registration of transfer of shares. Wherever registration of transfer has been refused the company has complied with the requirements of Section 111 of the Companies Act, 1956; and

(g) based on the information and explanations provided to me, the company has generally complied with all applicable provisions of the Companies Act, 1956.

II. I further report that

(a) approvals, if any, of authorities under the Monopolies and Restrictive Trade Practice Act, 1969 have been/have not been obtained by the company.

* Where approvals have not been received, make a note as to whether it is pending.
(b) the terms and conditions of orders, if any, passed by the authorities under the MRTP Act, 1969 have been complied with.

III. I further report that the company has/has not complied with the terms and conditions of the listing agreements.

IV. I further report that the necessary approvals have/have not been obtained from the Government/RBI under the FEMA in respect of foreign collaborations and technology transfer agreements, equity participation by foreign investors/NRI's, remittance of royalty/dividend/interest.

V. I further report that the necessary approvals have been obtained from the Government/RBI under the FEMA in respect of issue of shares and debentures and bonds, and payment of dividend/interest on them.

VI. I further report that various approvals under the pollution control laws have been obtained and that the directions issued by the statutory authorities have been complied with.

VII. I further report that the company has/has not obtained necessary approvals, and permission for exemption from applications of the provisions of important industrial and labour laws, has/has not maintained proper books and records, and has/has not given proper notices/filed proper returns with the statutory authorities and that the company has/has not complied with the various requirements of the labour laws.

VIII. The company has obtained financial assistance from___________ (Name of the Financial Corporation/Institution) and on verification of the terms of assistance vide agreement dated____________. I report that the company has complied with all the requirements of the terms/the company has not complied with the following terms viz.

IX. The above report is based on the information/records and registers made available to me/us as were found to the best of my/our knowledge to be necessary for the purposes of this Audit.

Signature of Company Secretary
C.P. No.____________

Place:
Date:

DECLARATION

I __________________________________________ a member of the Institute of Company Secretaries of India, do declare that I am a Secretary in whole-time practice as defined in Section 2(2) of the Company Secretaries Act, 1980 and hence am qualified to undertake Secretarial Audit of your company.

I do further declare that I do not suffer from any of the disqualifications set out in the Guidance Note issued by the Institute of Company Secretaries of India.

Signature
Certificate of
Name ______________________
SECRETARIAL AUDIT - PROCESS

Secretarial Audit is an area of practice for company secretaries which demands expertise and specialised and comprehensive knowledge of Companies Act, 1956 and laws relating to MRTP, SEBI regulations relating to capital issue, takeover code, insider trading, mutual funds, depositories and participants regulations, Foreign exchange/ collaborations etc. Such an audit involves a whole gamut of activities for a certain period in the past preferably on a year to year basis. The variety and complexity of the legal requirements that govern the day to day functioning of every industrial company, even of medium size and extent of concern and interest of various sections of society particularly of the investing public in the operation of companies, makes it essential that the process of secretarial audit should be undertaken with utmost care and diligence.

1. Before embarking on an assignment one should familiarise himself thoroughly with the relevant Acts, Rules, Regulations, Orders, Notifications, Guidelines, Clarifications and other material issued by the Government from time to time. It is expected that the Secretarial Auditor/Consultant will keep himself abreast of the latest developments in these areas so that he can render his services in an efficient manner.

2. Where the position of law is not clear, he should request the company to obtain legal opinion in order to be doubly sure about the compliances.

3. Where certain facts cannot be personally checked, he should obtain a certificate from the company in order to assure himself that proper compliances have been made. But where such detailed probe is not necessary, he should not insist on unnecessary information.

4. Judicial pronouncements of various Courts of the land also provide precedents. So the Secretarial Auditor should also keep himself abreast of latest judicial pronouncements on all important issues.

5. Private companies, government companies and Section 25 companies are exempt from some of the provisions of the Companies Act. These should be kept in view by the Secretariat Auditor. He should also keep himself abreast of the Rules, Regulations, Orders, Guidelines etc. framed under the Companies Act, the M.R.T.P. Act and other relevant legislations.

6. The Secretarial Auditor/Consultant should preserve the working sheets and other papers, the details of the documents inspected, prepared etc. for future reference and queries if any. This should be kept only for reference and should not be used for any other purposes. The minutes of board meetings relate to internal matters of a company and the Secretarial Auditor/Consultant should utilise the information only for carrying out his duties. Should the need arise, the Check-list/Working-sheet may be used to satisfy the queries of the Ministry of Corporate Affairs, Registrar of Companies or
the Monopolies and Restrictive Trade Practices Commission as the case may be.

7. While undertaking Secretarial Audit/Consultancy, as required, the following should be examined carefully:
   1. Memorandum and Articles of Association (Extent of applicability of Table A).
   2. Certificate of Incorporation.
   4. Annual Reports.
   5. Minutes Books of Board/Committee/General Meeting.
   6. Register of Members/Debentureholders.
   7. Register of Directors.
   8. Register of Loans, Guarantee, Security and Investments.
   9. Register of Charges.
   10. Foreign Register of Members and Debentureholders, if any.
   12. Register of Contracts.
   13. Register of Directors' Shareholdings.
   15. Correspondence with the Ministry of Corporate Affairs, Registrar of Companies, MRTP Commission, Ministry of Industry, Ministry of Finance, Stock Exchanges etc.
   16. Listing Agreement with the Stock Exchange.
   17. Register of investments of the company not held in its name.
   18. Register of Buy-back of Securities under Section 77A(9).
   19. Copies of various e-forms filed under Section 610B of the Companies Act, 1956.
   20. Various advertisements/press release issued by the company during the year.
   21. Other Registers as may be notified from time to time under various rules.

As soon as the assignment is over, the Secretarial Auditor should submit his report to the Board of Directors. He may submit interim reports also from time to time if necessary. The report should set out in detail the scope of the work, his observations on irregularities noticed, weakness in the policies and procedures etc. It should be drafted in the simple language, divided into paragraph.

**Appointment of Secretarial Auditor**

Prior to accepting the appointment, a company secretary in practice shall give a declaration to the company in the prescribed form that he is a Company Secretary in
practice as defined in Section 2(2) of the Company Secretaries Act, 1980, and that he does not suffer from any disqualifications set out in the guidelines:

**Periodicity of Secretarial Audit**

*Period of audit:* The Secretarial Audit would relate to the current financial year of the company. It may also cover a few years preceding the current year.

**Qualification/disqualification**

(i) *Qualifications:* Only a member of the Institute holding a certificate of practice can be appointed as a secretarial auditor.

(ii) *Disqualifications:*

(a) None of the following shall be qualified for appointment as secretarial auditor of a company:

(i) a body corporate;

(ii) an officer or employee of the company;

(iii) a person who is a partner, or who is in the employment of an officer or employee of the company;

(iv) a person who is indebted to the company for an amount exceeding ten thousand rupees, or who has given any guarantee or provided any security in connection with the indebtedness of any third person to the company for an amount exceeding ten thousand rupees;

(v) any person who ceases to be a Company Secretary in practice before submitting his Secretarial Audit Report.

(b) A person shall also not be qualified for appointment as secretarial auditor of a company if he is, by virtue of the above provisions, disqualified for appointment as secretarial auditor of any other body corporate which is that company’s subsidiary or holding company or a subsidiary of that company’s holding company, or would be so disqualified if the body corporate were a company.

(c) If a secretarial auditor becomes subject, after his appointment, to any of the disqualifications specified hereinabove he shall be deemed to have vacated his office as such.

(iii) *Reporting:* The secretarial auditor shall submit his report to the Board of Directors. At the option of the company the Secretarial Audit Report may be circulated to shareholders as Annexure to the Directors’ Report.

(iv) *Scheme voluntary:* It may be understood that the secretarial audit suggested above is purely optional for a company till a statutory provision is made in the Act. It is a welcome sign that some companies have recognised the benefits and have voluntarily arranged for such audit by a secretary-in-practice.

**Rights of Secretarial Auditors**

1. Right of access to various statutory books and other records.

2. Right of access to minute books, various forms, returns, documents and
copies of resolutions filed with Central Government, CLB, ROC, Official Liquidator or any other authorities.

3. Right to obtain information or explanation.

4. Right to receive notices of any general meeting of the company.

5. Right to attend the general meeting.

6. Right to remuneration.

**Social Responsibilities of Secretarial Auditors**

A business enterprise today is conceived as an amalgam of the interest of shareholders, creditors, employees, consumers, society and the public at large. In short, the corporate activities in a welfare State interact and affect the society at large. With the welfare concept of the State in view, several important pieces of legislations have been enacted in India, some of which are:

(viii) The Drugs and Cosmetics Act, 1940.
(xi) The Industrial Disputes Act, 1947.
(xii) The Workmen’s Compensation Act, 1923.

The Government seeks to achieve the goal of social welfare of the community by control and regulation of the corporate sector through the enactment of these economic and social legislations. Trade, commerce and industry have to operate within the framework of the increasing number of corporate and industrial laws, rules and regulations etc. Law is instrumental in effecting social reforms and public control of business. These social legislations try to harmonise the conflicting claims of individual interests, public interests and social interests. Success of any law is largely
dependent upon its implementation. Inadequate administration, poor monitoring and control of these social welfare laws, rules, regulations, orders etc. cannot achieve the desired objectives. It is in this context that a professionally qualified Company Secretary with sound comprehension of various intricate laws and procedures, through his Secretarial audit functions, give a practical shape to these enactments and ensure their compliance by the corporate sector.

The social responsibility of a Secretarial Auditor lies in effectively bridging the gap between the precept and practice of mercantile, economic and social legislation by the corporate sector. Being equipped with sound knowledge and understanding of these laws and governed by a Code of Conduct, a Secretarial Auditor owes a duty to the society to render expert legal opinion about the interpretation of the laws, rules and regulations, orders etc., by ensuring that the various agreements, contracts and other such documents drawn by the client company are in conformity with the provisions and spirit of laws to which these companies are subjected to; whether the concerned company has maintained various registers and records required to be maintained for the proper implementation and administration of these laws; whether the concerned Returns/Forms have been filed by the concerned company with the appropriate administrative/regulatory authorities; whether the company has furnished various data/documents with the various Government Departments as required; whether the company is following a sound labour/personnel policy as required under the provisions of various Labour Legislations, Rules, Orders, Regulations etc. made thereunder; whether the Company is regular in payment of various dues of the Financial Institutions and Banks in terms of specific Agreements entered in respect thereof; whether the Company is regular in paying its creditors and suppliers as per the terms and conditions of the relevant Agreements and whether the company is not indulging in frivolous litigations and deploying the funds of the company for such purposes; whether the company is serious and sincere in implementation of the orders of the Pollution Control Boards and other bodies entrusted with regulating the protection of environment; whether the company is following all those regulations which are aimed at consumer protection; whether the company is cooperating with Government in proper implementation of these mercantile, social and economic legislations etc.

These expectations of society and the Government from the profession of Company Secretaries on whom the job of Secretarial Audit is to be entrusted, include fearless dedication to the great cause aimed at ensuring and achieving the objective of a Welfare State. The Secretarial Auditor is expected to be above narrow motives of personal gains and to scientifically and professionally go about in ensuring the compliances of these various legislations by the companies, be they in the small scale sector or in the medium or in the large sectors of industry. Increasingly greater reliance will be placed on the Reports of the Secretarial Auditor by all concerned viz. The Company Management; Financial Institutions; Banks; Creditors and Suppliers; Shareholders; Registrar of Companies; Administrative/Statutorily appointed Authorities overseeing the implementation of these numerous legislations and above all by the Society at large. Hence, display of excellent professional and ethical standards by Secretarial Auditors will not only enhance the prestige of such persons but the prestige and goodwill of the Institute of Company Secretaries of India.

Compliance Certificate
As per the proviso to Section 383A(1) of the Companies Act, 1956 every company not required to employ whole-time company secretary under sub-section (1) and having a paid up share capital of ten lakh rupees or more but less than 2 crore rupees shall file with the Registrar a certificate from a practicing company secretary in such form and within such time and subject to such conditions as may be prescribed [See Companies (Compliance Certificate) Rules, 2001], as to whether the company has complied with all the provisions of this Act and a copy of such certificate shall be attached with Board’s report referred to in Section 217.

As per Section 383A read with Rule 2 of the Companies (Appointment and Qualifications of Secretary) Rules, 1988, every company having a paid up share capital of rupees 10 lakhs or more but less than rupees 2 crores is required to file with the Registrar of Companies, a compliance certificate from a company secretary in practice and also attach a copy of that certificate with the Board’s Report. In terms of proviso to Section 383A(1), the Central Government has prescribed the Companies (Compliance Certificate) Rules, 2001 for issue of Compliance Certificate by a practicing company secretary.

There is a very thin line of demarcation between Secretarial Audit and Compliance Audit and the terms are often used interchangeably. Secretarial Audit is wider in ambit and denotes a check on numerous legal compliances and also the process carried out by concerned company.

The scope of Compliance Certificate would comprise of certification of the compliance of various requirements under the Companies Act, 1956 and the rules thereunder. As a result, Compliance audit forms a part of Secretarial Audit and the checklist under the Companies Act, 1956 is prominently the same.

CHECK-LIST FOR SECRETARIAL AUDIT

SEBI Rules, Regulations, Guidelines

Some of the major guidelines/regulations which are to be looked into by a Secretarial Auditor:

(i) SEBI Guidelines


(ii) SEBI Regulations


In case of unlisted companies the Secretarial Auditor is required to look into the following regulations/rules, which may be relevant for a company:

**Forms, Returns and Documents to be Filed with other Authorities**

Secretarial Auditor should also, if required, check whether forms, returns and documents have been filed with the other authorities as mentioned below:

1. intimation has been given to the Company Law Board in respect of any default made by the company in repayment of any deposits from small depositors within 60 days from the date of default. Intimation shall be given on monthly basis;
2. copy of Return of Deposits of a non-banking non financial company has been filed with the Reserve Bank of India pursuant to Rule 10 of the Companies (Acceptance of Deposits) Rules, 1975;
3. text of advertisement inviting deposits by a non-banking financial company has been filed with the Reserve Bank of India pursuant to Rule 5 of the Non-Banking Financial Companies And Misc. Non-Banking Companies (Advertisement) Rules, 1977;
4. returns have been filed with the Securities and Exchange Board of India in case of buy-back of securities;
5. intimation required to be given to the Official Liquidator/Courts when the company is in the process of winding up/amalgamation/merger/reconstruction have been given.

**Monopolies and Restrictive Trade Practices Act, 1969**

1. **Enquiry into Monopolistic Trade Practices [Sections 10(b), 31 and 32]**
   
   (a) Check whether any enquiry has been instituted against the company in regard to alleged monopolistic trade practices indulged in by the company [Section 10(b) read with Section 31].
   (b) If yes, whether any orders have been passed against the company [Section 31(3)].
   (c) Whether the company challenged the orders so passed in appeal or otherwise. If yes, whether the orders have been stayed.
   (d) Whether the orders passed (unless they have been stayed or appealed against) have been complied with by the company.

2. **Registration of agreements relating to Restrictive Trade Practices (Section 33 read with Section 35)**

   (a) Check whether the company has entered into any agreement with any stockist/dealer containing any restrictions of the nature illustrated in Section 33(1).
   
   For exemption from registration check whether:
   
   — The agreement was expressly authorised under Section 38 of the Act.
   — The agreement has been expressly approved or authorised by the
Central Government.

☐ The Government is a party to such agreement?
☐ The agreement relates to appointment abroad in relation to exports.

(b) If yes, whether the agreement(s) have been registered with the Director General of Investigation and Registration [DG (I&R)].

(c) Whether any particulars of agreements have been registered/ordered to be registered in the Special Section of Register maintained by the DG (I&R) in terms of Section 36(2).

3. Enquiry into Restrictive Trade Practices [Section 10(a), 37 and 38]

(a) Check whether any enquiry has been instituted against the company against any alleged restrictive trade practice.

(b) If yes, what is the stage of the enquiry:
   (i) whether final orders passed;
   (ii) whether enquiry proceedings are in progress; or
   (iii) whether the company has agreed for a consent order.

(c) Where final orders have been passed by the MRTP Commission, whether the company has complied with those orders.

4. Enquiry into Unfair Trade Practices (Section 36A to 36E)

(a) Check whether any enquiry has been instituted against any alleged unfair trade practice.

(b) If yes, what is the stage of enquiry:
   (i) whether final order passed;
   (ii) whether enquiry proceedings are in progress; or
   (iii) whether the company has prayed for consent order.

(c) Where final orders have been passed by the MRTP Commission, whether the company has complied with those orders.

5. Injunction orders in respect of Monopolistic, Restrictive and Unfair Trade Practices (Section 12A)

(a) Check whether the MRTP Commission:
   (i) is considering any application for grant of interim injunction against alleged Monopolistic, Restrictive or Unfair Trade Practices; or
   (ii) has passed any interim injunction order.

(b) Where interim injunction order has been passed:
   (i) whether the company has complied with the order;
   (ii) whether the company has sought a stay of the order by resort to a Court of law; or
   (iii) whether the interim order has been vacated by the Commission during the regular enquiry.
6. Compensation claims against Monopolistic, Restrictive and Unfair Trade Practices (Section 12B)
   (a) Check whether any enquiry in respect of claim for compensation against Monopolistic/Restrictive/Unfair Trade Practices is pending before Commission.
   (b) If yes:
      (i) whether the Commission has dismissed the claim;
      (ii) whether the Commission has ordered payment of compensation; or
      (iii) whether the compensation awarded is under challenge in appeal or otherwise.

7. Resale price maintenance (Sections 39 and 40)
   Check whether any agreement with a retailer or wholesaler or any other dealer for sale of product contains any clause with regard to resale price maintenance.
   Check whether such agreements provide for withholding of supplies in case the stipulation with regard to re-sale price maintenance is not adhered to.

8. Furnishing information to Central Government under Section 43
   (a) Check whether the company is required to file with the Monopolies Research Unit two copies of annual report including the balance sheet and profit and loss account.
   (b) Check whether the company has been ordered to furnish information in the form prescribed in the MRTP (Information) Rules, 1971.

9. Penalty/prosecution proceedings (Sections 45 to 53)
   (a) Check whether any penalty/prosecution proceedings have been launched under the Act for violation of any provision(s) of the Act.
   (b) If yes:
      (i) what are the allegations;
      (ii) names of directors against whom prosecution has been launched; and
      (iii) the stage at which the prosecutions stand.

Securities Contracts (Regulation) Act, 1956

1. Listing may either be:
   (i) Initial listing;
   (ii) Listing of Public Issues;
   (iii) Listing of Rights Issues;
   (iv) Listing of Bonus Issues;
   (v) Listing of debentures and bonds;
   (vi) Listing of Preferential Issues.

Compliance:
(1) Check whether the company's securities are already listed on a Stock Exchange;

(2) Check whether the company has issued shares/debentures/bonds to the public. If yes, whether:

   (a) An application for this purpose to the stock exchange has been made along with the documents and particulars mentioned in Rule 19(1) of the Securities Contracts (Regulation) Rules, 1957;

   (b) Has the listing agreement been finalised and approved by the company's Board and executed with the stock exchange concerned. In case any conditions have been imposed by the stock exchange, have those restrictions/conditions been incorporated in the agreement.

   (c) Whether listing was done within the statutory time limit?

   (d) Where permission for listing has been refused by the Stock Exchange:

       ☐ Whether appeal was filed?

       ☐ What is the outcome of the appeal?

   (e) Whether all terms and conditions of the listing agreement have been complied with.

2. Compliance with the terms and conditions of the listing agreement:

Check whether the company has complied with the terms and conditions of the listing agreement. In particular, whether compliance relating to the following points have been carried out.

   (i) share transfers have been effected within the stipulated time period;

   (ii) the requirements of book closure have been complied with;

   (iii) the requirements of informing the Stock Exchange(s) regarding bonus or rights issues/dividend proposals complied with;

   (iv) Payment of dividend on shares, interest on debentures /bonds, redemption amount of redeemable shares or debentures/bonds;

   (v) the requirements of informing the Stock Exchange(s) regarding change in the composition of the Board of directors/managing director complied with;

   (vi) Further issue of Securities;

   (vii) Cash Flow Statement in the Annual Report, Consolidated Financial Statement and related party disclosures;

   (viii) Shareholding pattern containing details of promoters holding and non-promoters holding;

   (ix) Decision regarding issue of shares, forfeiture of shares, alteration of shares, cancellation of declared dividend, merger, amalgamation, de-merger, hiving off, voluntary delisting and other material decisions;

   (x) the Distribution Schedule has been filed with the Exchange(s);

   (xi) quarterly unaudited financial results have been published in newspapers and a copy of these results is sent to the stock exchange;
(xii) in any proposal to purchase shares of any other company, the requirements of clause 40A/40B of the listing agreement have been complied with;

(xiii) Half-yearly results and Limited review Report by auditors;

(xiv) Quarterly reporting of Segment wise Revenue, results and Capital Employed;

(xv) Consolidated Quarterly Financial results of holding company;

(xvi) the copies of annual accounts and notices of general meeting are regularly sent to the exchange;

(xvii) Change of name due to new activity;

(xviii) Explanation regarding variations in utilisation of funds and profitability;

(xix) Registration of share Transfer;

(xx) Loss of share certificate and issue of duplicate Certificate;

(xx) Amendments to Memorandum and Articles of Association are sent to the exchange(s);

(xxii) the exchange is informed of important events like, strike, lockout or amalgamation;

(xxiii) Clause 49 relating to Corporate Governance has been complied with;

(xxiv) Clause 50 relating to Accounting Standards.

**Foreign Exchange Management Act, 1999**

**Forms of Inbound Investments**

1. **Issue and Transfer of Shares to Non-Residents/NRIs under Foreign Direct Investment Scheme**

   In case of purchase of shares or convertible debenture of an Indian company by a person resident outside India, other than citizens of Bangladesh or Pakistan or Sri Lanka or an entity outside India whether incorporated or not (other than an entity in Bangladesh or Pakistan).

   Check whether □

   (i) the purchaser is a citizen of Bangladesh, Pakistan or Sri Lanka.

   (ii) the entity is an entity of Bangladesh or Pakistan.

   (iii) the person purchasing the share is a collaborator or proposes to acquire the entire shareholding of new Indian Company, if yes:

   (a) whether the prior permission of the Central Government has been obtained.

   (b) whether he has previous venture or tie-up in India through investment in shares or debentures or a technical collaboration or a trade mark agreement or investment in the same field or allied field in which the Indian company issuing shares is engaged.

**Automatic Route of Reserve Bank of India**
Check whether

(i) the Indian company is engaged in any activity included in the Annexure A to Schedule 1 of the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000.

(ii) such issue is within the limit specified in the above Regulations.

(iii) the provisions of Industrial Policy and procedure notified by the Secretariat for Industrial Assistance (SIA) is complied with.

(iv) the applicable provisions of IDRA are complied with.

(v) the activity of the issuer company requires an industrial licence.

(vi) the shares or convertible debentures are not being issued with a view to acquiring existing shares of Indian companies.

(vii) if the Indian company is a trading company, whether it has issued shares or convertible debentures only upto 51% of its capital and check that remittance of dividend to shareholders outside India is made only after the company has secured registration as an Export/Trading/Star Trading/Super Trading House from Ministry of Commerce.

(viii) the issuer company is a small scale industrial unit.

(ix) such small scale unit manufactures items not included in Annexure A of the aforementioned regulations, if yes:
    (a) check that the extent of such issue does not exceed 24% of its paid-up capital.
    (b) check the following items if such issue exceed 24% of its paid-up capital.
        —□ whether it has given up its SSI status.
        —□ the item it proposes to manufacture is not reserved for SSI.
        —□ it complies with the ceilings specified in Annexure B of the Regulations.

(x) the unit is a EOU or located in EPZ/FTZ/STP/EHTP. If yes, whether such issue exceed 24% of the paid-up Capital and whether the ceiling in Annexure B is complied with.

(xi) Check whether the shares have been issued within 180 days of receipt of remittance.

2. Issue of shares by a company requiring Government approval

Check whether:

(i) the approval of the SIA/FIPB has been obtained by the company in those cases where automatic route is not available;

(ii) company is eligible to issue ADR/GDR;
    (a) whether approval of the Ministry of Finance, Government of India has been obtained if such issue likely to exceed the limits prescribed for automatic approval; or
    (b) it is eligible to issue ADR/GDR in terms of relevant scheme in force;
(iii) the ADR/GDR are issued in accordance with the scheme for issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism Scheme), 1993 and Guidelines issued by the Government from time to time thereunder;

(iv) the details of the issue have been furnished to RBI in the specified form within 30 days of closure of in issue prescribed form;

(v) the company issuing shares against ADR/GDR has submitted Quarterly Return to RBI in the specified form within 15 days of the close of calendar quarter;

(vi) funds raised are repatriated to India, if not,
   - the company has invested the funds in deposits with or Certificate of Deposits or other instruments of banks who have been rated A1+ by Standard and Poor, Fitch, IBCA or Moody’s for short term obligations; or
   - deposited with branch outside India of an authorised dealer in India; or
   - invested in treasury bills and other monetary instruments with a maturity or un-expired maturity of the instrument of one year or less.

3. Issue Price

Check whether

(i) the issue price of shares issued to persons resident outside India is not less than the price worked in accordance with SEBI guidelines when the issuing company is a listed company.

(ii) fair valuation of shares done by a chartered accountant as per the guidelines issued by the erstwhile CCI, in all other cases.

(iii) in respect of ADRs/GDRs, if the issue is on public offer basis the price of ADRs/GDRs is decided by the Indian company in consultation with Lead Manager to the issue.

4. Rate of Dividend

Check whether the rate of dividend on preference shares or convertible preference shares has not exceeded 300 basis points over the Prime Lending Rate of State Bank of India prevailing as on the date of Board Meeting of the company in which issue of such share is recommended.

5. Mode of payment

Check whether the payment for such shares is received by remittance through normal banking channels or by debit to NRE/FCNR account of the person concerned maintained with an authorised dealer/authorised bank.

6. Report by Indian Company to RBI

Check whether the company has submitted necessary report in form FC-GPR to RBI within 30 days issue of shares.

7. Purchase of shares by NRI through a stock exchange under Portfolio Investment Scheme
Check whether

(i) the purchase is made through registered broker or recognised stock exchange;

(ii) the transactions have been routed through the designated branch of authorised dealer;

(iii) the paid-up value of shares purchased by NRI on repatriation and non-repatriation basis, does not exceed 5% paid-up value of shares issued by the company;

(iv) the paid-up value of each series of convertible debenture purchased by NRI on repatriation or non-repatriation basis does not exceed 5% of the paid-up value of each series of convertible debentures issued by the company;

(v) the aggregate paid-up value of shares purchased by NRIs has not exceeded 10% of the paid-up capital of the company;

(vi) — the aggregate paid-up value of each series of debenture purchased by all NRIs has not exceeded 10% of the paid-up value of each series of convertible debenture;

— the Special Resolution has been passed at the General Meeting if the limit has gone upto 24%;

(vii) the NRI has taken delivery of shares purchased and given the delivery of shares sold;

(viii) the payment has been made through inward remittance in foreign exchange through normal banking channels or out of funds held in NRE/FCNR account maintained in India in case of repatriation basis;

(ix) the payment has been made through inward remittance or out of funds held in NRE/FCNR/NRO account where the shares/debentures are purchased on non-repatriation basis.

8. Purchase of shares on non-repatriation basis other than under Portfolio Investment Scheme

Check whether

(i) the amount of consideration for purchase of shares or convertible debentures on non-repartriable basis has been paid by way of inward remittance through normal banking channels from abroad or out of funds held in NRE/FCNR/NRO account maintained with an authorised dealer or with an authorised bank in India.

(ii) the NRI is resident in Nepal and Bhutan, if yes, the amount of consideration for purchase of shares or debenture on repatriation basis is received only through inward remittance in foreign exchange through normal banking channel.

9. Acquisition of rights shares

Where a person resident outside India has purchased equity or preference shares or convertible debentures offered on rights basis, check whether

(i) the right offer has not resulted in the increase in percentage of foreign equity
already approved or permissible under Foreign Direct Investment Scheme,

(ii) the existing shares or debentures against which the shares or debentures are issued by the company on right basis were acquired and are held as per the provisions of Foreign Exchange Management (Transfer or issue of Security by a Person Resident Outside India) Regulations, 2000,

(iii) the offer price to person resident outside India was not lower than that at which the offer was made to resident shareholders,

(iv) the repatriability condition applicable to original shares has also been enclosed to rights shares,

(v) the amount of consideration has been paid by way of inward remittance through normal banking channels or by debit to NRE/FCNR account when the right shares or debentures have been issued on repatriation basis,

(vi) the amount of consideration has been paid by debit to NRO account in case the right shares/debentures has been issued on non-repartriable basis.

10. Issue and acquisition of Shares after Merger/Demerger or Amalgamation of Indian Companies

Check whether

(i) the merger/demerger or amalgamation of Indian companies has been approved by the High Court in India,

(ii) the percentage of shareholding of persons resident outside India in the transferee or new company has not exceeded the percentage specified in the approval granted by the Central Government or the RBI or specified in the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000,

(iii) in case, the percentage has exceeded the specified limit, the approval of the Central Government and RBI have been obtained,

(iv) the transferor or transferee company is engaged in agriculture, plantation or real estate business or trading in TDRs,

(v) the transferee or new company filed a report to RBI within 30 days giving full details of the shares held by persons resident outside India in the transferor and the transferee company before and after the merger/demerger/amalgamation/reconstruction.

(vi) the company furnished a Report to RBI confirming that all the terms and conditions stipulated in the scheme approved by the High Court have been complied with.

11. Issue of shares under Employees’ Stock Option Scheme to Persons Resident Outside India

In the case an Indian company has issued shares under the Employees’ Stock Option Scheme to its employees or employees of Joint Venture or wholly owned subsidiary abroad. Check whether

(i) the scheme has been drawn in terms of regulations issued under the Securities and Exchange Board of India Act, 1992,
(ii) the face value of the shares to be allotted under the scheme to the non-resident employees has not exceeded 5% of the paid-up capital of the issuing company,

(iii) the issuing company has submitted a report to RBI within 30 days containing the following particulars/documents:

- □ names of the persons to whom shares have been issued under the scheme and the number of shares issued to each of them,
- □ a certificate from the company secretary of the company that the value of the shares issued under the scheme has not exceeded 5% of the paid-up capital of the issuing company and the shares have been issued in compliance with the regulations issued by the SEBI.

12. Transfer of Shares and Convertible Debentures of an Indian Company by a Person Resident Outside India

In case a person resident outside India holding the shares or debentures of an Indian Company in accordance with the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000 has transferred the shares or debentures so held by him. Check whether

(i) the transferor, is a resident outside India and being a non-resident Indian or overseas body corporate and the transferee a person resident outside India,

(ii) A person being resident outside India, but not being a NRI or OCB has transferred by way of sale or gift, the shares or convertible debentures held by him or it to any person resident outside India. Also, whether an NRI has transferred shares/debentures to another NRI only.

(iii) the persons to whom the shares are being transferred has obtained prior permission of the Central Government to acquire the shares if he has previous venture or tie up in India through investment in shares or debentures or technical collaboration or a trade mark agreement or investment by whatever name called in the same field or allied field in which the Indian company whose shares are being transferred is engaged.

13. Prior Permission of RBI in Certain Cases for Transfer of Security

(A) Transfer by way of gift or sale by a person Resident in India

Check whether

(i) the transfer was by way of gift or sale,

(ii) the transferor was a person resident in India and the transferee resident outside India not being erstwhile OBCs,

(iii) in case of transfer by way of gift, an application has been made to RBI furnishing the following information:

- □ Name and address of the transferor and proposed transferee,
- □ Relationship between the transferor and the proposed transferee,
Reasons for making the gift.

(iv) In case of sale of shares/convertible debentures:
- whether the activities fall under Annexure B to Schedule 1, other than items 1, 2, 3,
- sectoral limits have been observed,
- approval of the Central Government has been obtained,
- approval of the RBI has been obtained.
- whether Indian company is engaged in rendering any financial service;
- whether the transfer falls within the purview of provisions of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997; and
- whether the concerned parties adhere to pricing guidelines, documentation and reporting requirements specified by RBI.

(B) Transfer by way of sale by person resident outside India to Resident Indians

If a person resident outside India transfers shares or convertible debentures of Indian company, without RBI permission by way of sale, whether the pricing guidelines, documentation reporting requirements etc. as specified by RBI have been complied with.

Forms of Outbound Investments

Outbound Investments under this Act could be in any one of the following forms:

I. DIRECT INVESTMENT OUTSIDE INDIA (FOR AN INDIAN PARTY) i.e. BY A COMPANY INCORPORATED IN INDIA OR BODY CREATED UNDER AN ACT OF PARLIAMENT
(a) Investment in JV/WOS
(b) Agricultural operations overseas
(c) Investment in Equity of a Company registered overseas
(d) Investment in financial service sector
(e) Investment in foreign company by swap or exchange of shares of an Indian Company
(f) Investment by capitalization of receivables
(g) Investment in a foreign entity engaged in real estate business or banking business
(h) Acquisition of foreign company through bidding/tender
(i) Indian Party not satisfying eligibility norms for cases in a, b, c, d and e above
(j) Overseas investments by
   — corporates
   — individuals
(k) Investments abroad by mutual funds
(l) Direct Investment in Nepal or Bhutan in Indian Rupees

II. OTHER THAN DIRECT INVESTMENT

(a) Purchase/Acquisition of foreign securities by a resident individual in certain cases
(b) Transfer of foreign security by a person resident in India
(c) Acquisition of foreign security by a person resident in India being individual with specific approval of RBI

III. ACQUISITION AND TRANSFER OF IMMOVEABLE PROPERTY OUTSIDE INDIA

IV. INSURANCE

V. INDIAN DEPOSITORY RECEIPTS

The Secretarial Auditor has to check whether the procedures prescribed under each of the above heads have been followed.

Drawal of foreign exchange

The Secretarial Auditor is required to look at the Foreign Exchange Management (Current Account Transactions) Rules, 2000 to

— Check whether any foreign exchange is drawn for the purposes which are prohibited under Rule 3.
— Check whether prior approval of the Government of India is obtained for the transactions specified under Rule 4.
— Check whether prior approval of Reserve Bank is obtained for the transaction specified under Rule 5.

Water (Prevention and Control of Pollution) Act, 1974

1. Restriction on the applicability of the Act (Section 19)

Whether the State Government has restricted the applicability of the Act to the Area in which the manufacturing operations are carried on.

2. Directions regarding abstracting water from any stream or well, as also discharge of sewage and effluents (Section 20)

Whether directions, if any, regarding

(i) abstracting water from any stream or well; or
(ii) discharging sewage or effluents into any stream or well,
(iii) furnishing information regarding the construction, installation or operation of any establishment or any disposal system or any extension or addition thereto,

have been complied with by the company.

3. Discharge of polluting matter (Section 24)

Whether pollutant matter is being discharged into a stream or well or sewer or on land.
4. Consent of the State Board for new outlets and discharges (Sections 25, 27 and 28)
   (a) Whether consent of the State Board has been obtained for
      (i) establishing any industry/operation/process or any treatment and
disposal system or any extension or addition thereto which is likely to
discharge sewage or trade effluent into a stream or well or sewer or on
land
      (ii) bringing into use any new or altered outlet for discharge of sewage,
      (iii) beginning to make any new discharge.
   (b) Whether application for consent is made in specified form and if so, whether
terms and conditions of the consent have been complied with.
   (c) Whether consent given earlier by the State Board has been withdrawn.
   (d) If so, whether an appeal has been filed by the company.

5. Furnishing of information regarding discharge of effluents due to accident, etc.
   (Section 31)
   (a) Whether any noxious or polluting matter was discharged or likely to be
   discharged into a stream or well, due to accident or other unforeseen act or
event.
   (b) If so, whether information regarding the same was given to the State Board
and other specified agencies.

6. Orders of restraint by courts (Section 33)
   (a) Whether any court order has been made restraining the company from
causing any pollution by disposal of any matter.
   (b) If so, whether the terms of the Court Order have been complied with.

7. Directions of the Board (Section 33A)
   (a) Whether the Board has issued directions in writing to any person officer or
authority including a direction for closure, prohibition, regulation of any
industry, operation process or service etc.
   (b) If so, whether the directions have been complied with.

8. Prosecution/penalties (chapter VII)
   Whether prosecution proceedings have been initiated or penalties levied on the
company and/or its directors for violation of any provisions of the Act.

Air (Prevention and Control of Pollution) Act, 1981

1. Prohibition on use of certain appliances in declared areas (Section 19)
   (a) Whether any notification has been issued under Section 19 declaring the
area in which the premises of the factory of the company is situated, as air
pollution control area.
   (b) If so, whether directions, if any, of the State Government concerned
regarding use of approved appliances have been complied with.
2. Previous consent of the State Board for operating industrial plants (Section 21)
   (a) Whether previous consent of the State Board has been obtained for establishing or operating any new industrial plant set up by the company.
   (b) Whether the conditions of consent have been complied with.
   (c) Whether consent given has been cancelled. If yes, what action has been taken by the company on the matter.

3. Emission of air pollutants conform to the standards (Section 22)
   Whether the air pollutants emitted conform to the standards prescribed by the State Government.

4. Restraints on causing air pollution (Section 22A)
   (a) Whether any Court has been made orders restraining the company in regard to emission of any air pollutant.
   (b) Whether the state board has been authorised to implement the court’s direction in a specified manner.

5. Information to be furnished to the State Board etc. (Sections 23, 24, 25, 26)
   (a) Whether information, if any, has been given to the State Board regarding emission or apprehended emission of any air pollutant in excess of the standard laid down.
   (b) Whether any inspection has been carried information called or samples have been taken by the state board or any officer empowered by it.

6. Appeals (Section 31)
   Whether any appeal has been preferred by an aggrieved person against the orders of State Board.

7. Compliance with directions issued by the Central/State Board(s) (Section 31-A)
   (a) Whether any directions have been issued by the Central/State Board(s), particularly in regard to
      (i) closure, prohibition or regulation of any industry operation or process; or
      (ii) the stoppage or regulation of supply of electricity, water or any other service.
   (b) If so, whether such directions have been complied with.

8. Prosecution of company and its directors (Chapter VI)
   (a) Whether prosecution proceedings have been initiated against the company and its directors for violation of any provisions of the Act.
   (b) If yes, what is the stage/result of such proceedings.

Environment Protection Act, 1986

Emission Standards (Section 8)
— Whether the safeguards in respect of handling of hazardous substances
have been complied with information to be furnished (Section 9).

— Whether information regarding the discharge or apprehended discharge of an environmental pollutant in excess of prescribed standards has been furnished to the authorities and agencies.

— Entry, Inspection etc. (Section 10H) whether the powers of entry, inspection and taking of samples is exercised and due cooperation is extended to authorised officials.

— Prosecution of company and its directors (Section 16)
  (a) whether prosecution proceedings have been initiated against the company and its directors for violation of any provisions of the Act.
  (b) if yes, what is the stage/result of the proceedings.

Environment Audit Report [Rule 14 of Environmental (Protection) Rules]

Whether environmental Audit Report is required to be submitted.

In case, yes, whether the same relating to a financial year ending on 31st March has been submitted by the 15th May of the following year.

Select Industrial and Labour Laws

I. The Payment of Bonus Act, 1965

  (i) Check whether the Act is applicable to the company, in terms of Section 1 read with Section 32 of the Act.

  (ii) In the case of a newly established company, check the eligibility of employees for bonus in terms of Section 16 of the Act.

  (iii) If payment of bonus has become mandatory, check whether computation of gross profits, available surplus and allocable surplus has been made as per the provisions of the Act.
    (a) Check whether any settlement has been entered into with the employees for payment of Bonus, and
    (b) Bonus has been paid in accordance with the settlement and the amount is not below the minimum paid under the Act.

  (iv) Check whether the amount to be paid by way of bonus to an employee under the Act has been paid within the time limit prescribed under Section 19 of the Act.

  (v) Check whether the employer has prepared and maintained such registers, records and other documents as are required to be maintained under Section 26 of the Act read with Rule 4 of the Payment of Bonus Rules, 1975.

  (vi) Check whether during the period under review, any show cause notice/prosecution, etc., has been received/launched against the company and, if so, brief particulars thereof may be given.

II. The Payment of Gratuity Act, 1972

  (i) Check whether the Act is applicable to the company, in terms of Section 1 read with Section 5 of the Act.
(ii) Check whether the employer has determined the amount of gratuity payable to eligible employees in terms of Section 7 of the Act and has complied with the requirements of that Section.

(iii) Check whether the employer has complied with the requirement of giving the notice of opening, change, or closure of the establishment as may be applicable, as stipulated in Rule 3 of the Payment of Gratuity (Central) Rules, 1972.

(iv) Check whether the employer has displayed a notice specifying the name and designation of the officer authorised to receive notice under the Act or the Rules as required under Rule 4.

(v) Check whether the gratuity payable under the Act during the year under review has been paid in cash or, if so authorised by the payee, by demand draft or bank cheque to the eligible employees, nominees, heirs, as the case may be, as provided in Rule 9 of the Payment of Gratuity (Central) Rules, 1972.

(vi) *Check whether the employer has obtained an insurance in the manner to be prescribed, for his liability for payment towards the gratuity as provided in Section 4A of the Act.

(vii) Check whether, during the period under review, any show cause notice/prosecution, etc., has been received/launched against the company and if so, brief particulars thereof may be given.

III. The Factories Act, 1948

(i) Check whether the State Government concerned has made any rules under Section 6 of the Act in regard to approval, licensing, registration of factories. If so, ensure that the same have been complied with.

(ii) Check whether the provisions of Section 7 of the Act have been complied with by the occupier.

(iii) Check whether the company has complied with the requirements of the Act in regard to Health, Welfare and Safety of the workers employed in the factory of the company as stipulated by the Act read with the Rules made by the State Government concerned in this behalf.

(iv) Where any hazardous processes are carried on in the factory of the company, check whether the provisions as contained in Chapter IV-A of the Act in that behalf are complied with, especially with regard to Sections 41A, 41B, 41C, 41F, 41G and 41H of the Act.

(v) Check whether the provisions relating to working hours of adults, employment of young persons, etc., have been complied with.

(vi) Check whether notices in regard to certain accidents, dangerous occurrences, certain diseases, etc., have been properly given, as provided in Sections 88, 88A and 89 of the Act.

*Note: Section 4A introduced by the Payment of Gratuity (Amendment) Act, 1987 is yet to be brought into force. Therefore, the aspect mentioned in item (vi) has to be ensured after Section 4A is brought into force.*
(vii) Check whether a notice containing such extracts of the Act and the Rules made thereunder as may be prescribed has been displayed in the factory along with the names and addresses of the inspector and the certifying surgeon, as per Section 108 of the Act.

(viii) Check whether all such returns, whether periodical or occasional, as prescribed under the rules framed by the State Government, have been filed in time with the proper authorities under the Act, as required by Section 110.

(ix) Check whether during the period under review, any show cause notice/prosecution has been received/launched against the company and, if so brief particulars thereof may be given.

IV. The Employees’ Provident Funds and Miscellaneous Provisions Act, 1952

Check whether the Act is applicable and/or whether exemption has been obtained under Section 17A of the Act.

A. The Employees’ Provident Funds Scheme, 1952

(i) Check whether the employer has sought the particulars concerning the persons covered by the Scheme and their nominees in Form II and whether such particulars are entered in the declaration form, and that signatures or the thumb impressions of the persons concerned have been obtained.

(ii) Check whether the employer has prepared a contribution card in Form 3A and whether any employee has become a member of the Pension Scheme, 1995. If so, the aforesaid Form should also contain such particulars as are necessary to comply with the requirements of that Scheme.

(iii) Check whether all contribution cards are kept in safe custody and also whether any member or his representative is permitted to inspect his card on the request of the member.

(iv) Check whether particulars of all branches and departments, occupiers, directors, manager or any other person/persons who have the control over the affairs of the factory or establishment, have been furnished in duplicate to the Regional Commissioner in the prescribed form. Also check whether changes if any, in such particulars have been sent within 15 days of the change to the Regional Commissioner by registered post or in any such other manner as may be specified by the Regional Commissioner.

(v) Check whether the contribution payable by the employer under the scheme has been paid at the rates specified and as per the stipulations contained in paragraphs 29 and 30 of the Scheme. Check whether the monthly return in Form 5 in respect of employees qualifying to become members of the fund for the first time during the preceding month, together with the declaration in Form 2 as furnished by such employees has been sent to the Commissioner within 15 days of the close of each month.

(vi) Check whether the return in the prescribed form has been sent to the Commissioner in respect of employees leaving the services of the employer during the preceding month, and also ensure that a NIL return has been sent, if there is no employee qualifying to become a member of the Fund or there is no employee leaving the services of the employer during the preceding
B. The Employees' Pension Scheme, 1995

(i) Check whether the employer has remitted to the Pension Fund the contributions payable by himself each month, under Section 6A of the Act, as prescribed in the Scheme.

(ii) Check whether the employer has prepared contribution cards as per the Scheme.

(iii) Check whether particulars of ownership as well as changes in that regard have been sent to the Regional Commissioner as stipulated in Paragraph 16 of the scheme. Check whether a monthly return of the employees who are to join the Scheme every month has been submitted.

(iv) Check whether all the books, records and registers required to be maintained under the scheme are maintained properly.

C. The Employees' Deposit-Linked Insurance Scheme, 1976

(i) Check whether the employer has correctly calculated the contribution payable by him under Section 6C(2) and (4) of the Act.

(ii) Check whether the employer has made the payment of contribution within 15 days of the close of every month.

(iii) Check whether the employer has maintained proper accounts in relation to the amounts contributed to the Insurance Fund as directed by the Central Board from time to time.

(iv) Check whether during the period under review any show cause notice/prosecution has been received/launched against the company, and, if so, brief particulars thereof may be given.

(v) Check whether the company or any employee or class of employees is exempted from all or any of the provisions of any Scheme constituted under the Act. If so, check whether the company has complied with all the requirements subject to which exemption has been granted under Section 17 of the Act.

(vi) Check where applicable whether the company has complied with the public liability insurance in respect of handling dangerous chemicals.

Compliance with the Covenants Imposed under the Loan Agreement Entered into with the Financial Institution(s)

I. Operations

Check whether the following have been ensured, about the operations of the company:

(a) the company has not ceased to carry on business, even temporarily;

(b) any material changes in the operations, including creation of a subsidiary, implementation of expansion programmes, and undertaking any general trading activities have been approved by the financial institution;

(c) the registered office/location of the factory has not been shifted without the
prior consent of the financial institution;

(d) the name/constitution of the company has not been altered/changed without prior consent;

(e) the selling/purchasing agency has been given on terms and conditions laid down in the indenture. Where required the existing arrangements have been suitably modified. Specific permission has been taken where agreement is being entered into with the associate concerns of the promoter(s)/director(s) of the company; and

(f) any arrangements required to be entered into, as per the provisions of the indenture, have been duly made.

II. Security

Verify the following as regards security offered on the term loan, and subsequent acquisition of assets:

(a) all assets purchased subsequent to the loan agreement are the absolute property of the company;

(b) assets purchased from the money advanced/to be advanced, if not brought upon/fixed to the factory premises, have been hypothecated with the financial institution/commercial bank;

(c) the mortgaged premises and every part thereof, has been maintained in good and working order, and no part/item has been removed therefrom.

Any plant/item/part removed, has been replaced by plant/item/part of equivalent nature and value, unless it has become redundant, worn out or obsolete;

(d) the company has repaired/replaced any part of the land and building and all component parts thereof, as required and within the time period, specified by the financial institution;

(e) no other mortgage, lien or charge has been created on the mortgaged premises, other than that in favour of the financial institutions;

(f) the mortgaged plant/machinery has not been lent out/hired, nor has the land/building let out;

(g) where the mortgaged premises has been taken up by the Government or by a public body, entitled to do so, the proceedings for ascertainment and appointment of the compensation payable, have commenced;

(h) the company has not entered into any arrangement with the creditors, nor has any act or default been committed, as would render the company liable to be taken into liquidation;

(i) where guarantees have been furnished, in the event of death of a guarantor, his heirs have not given notice of revocation; and

(j) in the opinion of the assessors/valuers appointed by the company the value of the security has not become insufficient or depreciated beyond norms prescribed in the indenture.
III. Default in payment of interest/principal instalments

Confirm that in the event of default:

(a) the consent of the financial institution has been taken, where required, prior to distributing dividends and making interest payment on unsecured loans and deposits; and

(b) sales tax refunds/sum received from incentive schemes etc., have been applied towards payment of overdue amounts.

IV. Insurance

Check the following in regard to compliance of terms of insurance:

(a) the company's assets have been insured comprehensively. Where a joint insurance on plant and buildings has been taken, the value thereof has been apportioned in the manner prescribed/approved;

(b) the insurance policy has been taken in the joint names of the company and the financial institution;

(c) the policy has been kept alive for such full value, as has been determined by the financial institution, all premia are being paid in time, and the company has not done any such act as would render the policy void or voidable;

(d) the policy has been taken from an insurance office of repute, as determined by the financial institution; and

(e) all moneys received under the insurance policies are held in trust for better securing to the financial institutions, the payment of all moneys secured under the indenture agreement.

V. Information

Verify that the periodical statements required to be submitted to the financial institution, are being furnished in time. The statements may be on the operations of the firm/implementation of the project undertaken.

VI. Utilisation of Moneys Advanced

Ensure that consistency has been maintained in utilisation of moneys advanced to the mortgagor. The following aspects may be specifically examined:

(a) funds have been utilised for the purposes laid down in the indenture. Where funds have not been so utilised, the requisite permission has been taken;

(b) requisite conditions laid down to qualify for the outstanding balance of the loan have been fulfilled;

(c) the drawings from the loan are being kept in a separate Scheduled Bank Account, payments therefrom are being made in the manner laid down in the indenture, the said scheduled bank has foregone its right to set-off or lien, in respect of the said account, and the mortgagor is maintaining the records pertaining to the said account, as provided in the indenture;

(d) no part of the loan moneys has been transferred to call, short term, fixed or any other deposits, without prior consent. Where such consent has been
obtained, the scheduled bank has foregone its rights to set off any amount due from the company, against the deposits, the deposits have been realised on their due dates and the proceeds thereof re-deposited in the special account;

(e) the expenditure has been financed in the manner provided for in the indenture; and

(f) any changes/deviations in the time schedule for completion of the project have been made in consultation with the financial institution.

VII. Liabilities/Dues

Ensure as regards payment of liabilities/dues that:

(a) the company has been paying all the ground rents, rates, taxes*, dues, duties and outgoings immediately on their becoming due. Satisfactory provisions have also been made for meeting tax liabilities for subsequent years;

(b) where the company has any account(s) with bank(s)/financial institution(s), guaranteed by Reserve Bank of India, no default has been committed on its maintenance, as would render Reserve Bank of India liable to reimburse the guaranteed amount;

(c) any prepayments, of any amount other than the term loan and the bank borrowings in the ordinary course of business, have been made with the prior approval, in writing, of the financial institution. Any other conditions stipulated under the indenture, have also been complied with; and

(d) no other financial institution(s)/bank(s) with whom the company had entered into agreements for financial assistance have refused to disburse the loan(s) or any part thereof, nor have they recalled the sums disbursed under their respective loan agreements entered into with it.

VIII. Books of Accounts

Scrutinize the books of accounts to check that:

(a) proper books of accounts have been maintained by the company, in consonance with the requirements laid down in the Companies Act, 1956;

(b) books of accounts have been properly posted up at all times; and

(c) annual audit of the books of accounts has been conducted in the manner provided for under the Companies Act, 1956, and copies of audited accounts have been submitted to the financial institution within six months from the date of closing of the accounts.

IX. Share Capital

Confirm compliance of the following as regards capital structure:

(a) a capital structure of the company has not been alerted, without the written consent of the financial institution;

(b) the financial institution was intimated of the resolutions passed by the Board

* include income-tax, corporation tax, sales tax, provident fund contribution, ESI contribution, etc.
of Directors to make the calls on shares issued;
(c) all moneys received from the members in advance of calls upon the shares, are held in trust for the financial institution so as to form security under the indenture;
(d) moneys received on account of calls made/issue of shares were held for the specific period of time, and were utilised only subsequent to the financial institution defaulting on directions regarding application of such moneys towards satisfaction of the moneys due to it;
(e) any directions issued by the financial institution, as regards further issue of share capital/calls on shares issued have been complied with; and
(f) proposals for the approval of transfer of the company's shares (i) from the promoter's group to others and (ii) by persons, who have given 'non-disposal of shareholding' undertaking, have the approval of the financial institution.

X. Memorandum/Articles of Association
(a) Verify that any alteration in the Memorandum/Articles of Association has been made with the prior consent, in writing, of the financial institution.
(b) Confirm that the alterations/additions to the Articles of Association, as required under the indenture have been accordingly incorporated.

XI. Directors/Promoters
Scrutinise the records to ascertain that:
(a) the shareholdings of the directors have not been varied, nor have the deposits/unsecured loans received from the directors been reduced, without the prior consent of the financial institution;
(b) funds procured from the promoters/directors are only subject to such conditions as are laid down in the indenture;
(c) all amounts payable on account of any sitting fees, expenses, commissions, and remuneration to nominee directors, have been duly paid;
(d) no commission has been paid to the promoters, directors, managers or any other persons for furnishing guarantees, counter guarantees, obligations, indemnity or for undertaking any other liability/others, without the prior approval of the financial institution; and
(e) prior approval of the financial institution has been taken for the appointment/re-appointment of managing director/whole-time director/chairman/consultants, and as regards changes in their terms of appointment, except where these are as per the provisions of the Companies Act, 1956. The appointments, where necessary, have the approval of the Central Government.

XII. Board Meetings
Verify that all important matters, including those specifically required by the financial institution, were submitted for decision to the Board of directors and the meetings thereof were both called and conducted, in the manner laid down in the indenture.

XIII. Leasing and Trading Activities
Confirm that the power of leasing has been exercised, only with the prior consent of the financial institution, and subject to conditions laid down in the indenture. Where the mortgage deed is silent, the following conditions must have been satisfied:

(a) the lease has been made in the ordinary course of management of the property concerned, and the lease is in accordance with the local law, custom and usage;
(b) the lease has reserved the best rent that can reasonably be obtained. No premium has been received or promised, and no rent has been received in advance;
(c) the lease does not contain a covenant for renewal;
(d) the lease has taken effect from a date not later than six months from the date on which it was made; and
(e) the duration of the lease of building or any part thereof whether leased with or without the land or which it stands, does not exceed three years. The lease does not contain any covenant for payment of the rent, and a condition for re-entry on the rent not being paid within a time therein specified.

XIV. Technical Experts

Check whether the provisions contained in the indenture, as regards the appointment of experts, their technical training and any other directions, have been complied with, and the financial institution is being duly kept informed of such compliance.

XV. Licences/Consents

Ensure that the following licences/consents have been obtained:

(a) the registration/licences/renewals required under the Industries (Development and Regulation) Act, 1951/Foreign Exchange Regulation Act, 1973*, if necessary;
(b) the rights, powers, privileges, concessions, trade marks, patents and licence agreements necessary in the conduct of the business, have been renewed; and
(c) in case of SSI unit, the Registration has been renewed.

XVI. Contracts

Ensure that any structures as regards agreements for supply of plant and equipment, have been complied with, and competitive tenders have been called for, where required.

XVII. Legal Proceedings

Verify, as regards possible legal proceedings, that:

(a) the financial institutions had been intimated of any notices received under any Act, including the application for winding up under the Companies Act, 1956;
(b) where a receiver has been appointed on any of the properties/business

* Since repealed. FEMA, 1999 had been introduced in place of FERA.
undertaking of the company, or any distress or execution has been allowed to be levied on the mortgaged premises, the financial institution has been intimated about it; and

(c) the mortgagor is not party to any litigation of a material character.

XVIII. Takeover of Management

Verify in cases where the management of the company has been taken over by the financial institution:

(a) the shareholders of the mortgagor company have not nominated/appointed any person to be a director of the said company;

(b) no resolutions passed at the meetings of the shareholders, have been given effect; and

(c) no proceedings for winding up have been commenced, nor has any receiver been appointed without the prior consent of the financial institution.

XIX. Financial Position

Check the financial position to ensure that:

(a) the company has not put its funds, nor invested them in purchase of shares of any other concern, without the prior approval of the financial institution;

(b) no circumstances have occurred, as are likely to prejudice/imperil/depreciate the security of the financial institution;

(c) there is no reason to believe that it would be advantageous to commence liquidation proceedings against the company, or to take possession of the mortgaged premises;

(d) the company has made arrangements for raising the balance amount of Rs.______________ required under the project scheme through ______________ sources (specify);

(e) the company is in a sound financial position and there is no reason to apprehend that it would be unable to pay debts;

(f) no money has been withdrawn from the business, out of the capital or in anticipation of profits, without prior consent of the financial institution; and

(g) proposals to undertake inter-corporate loans or other investments, have the prior approval of the financial institution.

XX. Others

Check the following additional points to confirm that:

(a) further funds have not been borrowed from financial institution(s) on hundis, other than from its bankers, without prior consent;

(b) the term loan outstanding, has not exceeded the net effective capital together with free reserves, and deposits of the company. The company has also maintained during the currency of the loan, the minimum required margin, between the present market value of the mortgaged premises exclusive of the goodwill and the amount of loan outstanding, along with the interest
thereof;
(c) no donations/contributions have been made to the charitable and other funds, which are not directly related to the business of the borrower or to the welfare of its employees, in excess of the amount specified in the indenture, without the consent of the financial institution; and
(d) no merger/consolidation/re-organisation/arrangement/compromise with the creditors/shareholders has been undertaken/permissioned without the approval of the financial institution.

XXI. Certificate

Verify that the company has issued the Compliance Certificate in the prescribed format as required by the financial institutions.

LESSON ROUND-UP

- Secretarial Audit comprises of verification of compliance with rules, procedures, maintenance of books, records etc. by an independent professional to monitor compliance with various legal requirements.
- Secretarial audit not only ensures that the company has complied with the provisions of various laws but also extends professional help to the company in carrying out effective compliances and establishment of proper systems with appropriate checks and balances.
- Secretarial Audit can prove to be an effective and multipurpose mode to assure the regulator, generate and repose confidence amongst the shareholders, creditors and other stakeholders in companies, assure Financial Institutions, including state level Financial Institutions etc. and instill self regulation and professional discipline in companies.
- Secretarial audit is of immense utility even to larger companies which otherwise have a whole-time Company Secretary in its employment.
- Secretarial Audit Report is a report which the Secretarial Auditor shall prepare in relation to a company whose secretarial compliances are seen by him with respect to the maintenance of statutory registers, minute books, meetings of the company, approvals required from various authorities under the Companies Act, Monopolies and Restrictive Trade Practices Act, etc.
- Secretarial Audit is an area of practice for company secretaries which demands the expertise and specialised and comprehensive knowledge of Companies Act, 1956 and laws relating to MRTP, SEBI, regulations relating to capital issue, takeover code, insider trading, mutual funds, depositories and participants regulations, Foreign exchange/collaborations etc.

SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answers to these are not to be submitted for evaluation)

1. Discuss the need for and scope of Secretarial Audit.
2. State the guidelines evolved by the Institute for appointment of Secretarial Auditor.
3. What are the points to be kept in mind by the Secretarial Auditor while conducting Secretarial Audit of the company.

4. What all points are to be appraised while checking the compliance of a listed company?

5. Discuss the covenants imposed under the loan agreement entered into with the Financial Institutions.
LEARNING OBJECTIVES
The objective of this study lesson is to enable the students to understand
Meaning, Need, scope of Share Transfer audit
Appraisal of share transfer work
Salient features of listing agreement pertaining to share transfers
Audit for reconciliation of the total admitted capital with both the depositories and the
total issued and listed capital etc.
Safeguards on transfer of securities in dematerialised mode.

I. INTRODUCTION
Transferability of shares is one of the most vital features of a company limited by
shares. It is this attribute of a share that endows a company with perpetual and
uninterrupted existence. Upon incorporation, a company acquires its own
independent legal personality and distinct entity, and its shareholders acquire the
right to hold and transfer their shares in the company. Section 82 of the Companies
Act, 1956 states that the shares shall be movable property and transferable in the
manner provided by the articles of the company. It has, however, been consistently
held by the Courts that subject to the restrictions imposed by the articles, a
shareholder is free to transfer his shares to a person of his choice and that articles
cannot impose unreasonable restrictions on the right to transfer. Also, the directors
cannot decline to register a transfer arbitrarily or unreasonably.

II. NEED AND SCOPE
Registration of transfer of shares, debentures and other securities is one of the
area which has to be constantly monitored by the Company Secretary in a company.
This is one area where the investors have interaction with the company and also
judge its functioning. By not caring or not paying proper attention to the work
connected with registration of transfers the company whether manual or electronic
transfer, will have disgruntled shareholders. Naturally this will create a bad
impression on them and consequently the image of the company would suffer.

Under Section 108 of the Companies Act, 1956 a company cannot register a
transfer unless proper instrument of transfer duly stamped and executed by or on
behalf of the transferor and by and on behalf of the transferee and specifying the
name, address and occupation, if any, of the transferee is delivered to the Company
with the certificate relating to the security involved in transfer or where no certificate is
in existence, alongwith the letter of allotment of the security concerned. The transfer
deed will have to be in Form 7B appended to the Companies (Central Government’s)
General Rules and Forms, 1956. If the transfer deed relates to transfer of shares it
should be stamped with date by the Registrar of Companies or other officials
authorised in this behalf by the Central Government before anything is written on it.
The transfer deed so stamped is valid for lodgement in the case of a listed company within 12 months of the date so stamped or first closure of the register of members after it is so dated-stamped, whichever is later. In the case of an unlisted company it is valid for lodgement within two months of the date so stamped. The date-stamping requirement is not applicable in relation to transfer deed executed for transfer of debentures or other securities in a company. Transfer Deed duly executed for the registration of a transfer of the shares or other interest of a member in a company may be submitted either by the transferor or by ‘transferee’, together with the relevant share certificates. Where the validity period of an instrument of transfer has expired namely, the instrument is beyond 12 months from the date of presentation to the prescribed authority or from the date of book closure whichever is later in case of shares of a listed company, and in other case 2 months from the date of presentation, the holder may make an application in Form 7C to the Registrar of companies requesting for extension in validity, along with requisite fee based on the nominal value of shares.

Under Section 113 of the Companies Act, a company is required to deliver the certificate within three months after the allotment of any of its securities and within two months after the application for registration of transfer of any such securities. However, this period for issue of certificates for debentures may be extended by the Company Law Board*, on an application being made to it in this behalf by the company to a further period of not exceeding nine months where it is satisfied that it is not possible for the company to deliver such certificates within the said periods. Generally, the practice is to send the certificate to the person who lodged the transfer in question with the company or as per the instructions at the time of lodgement of the transfer deed for registration. Also see Jagatjit Industries Ltd. and others v. Mohan Meakin Ltd. and others (1991) 6 CLA 22 (CLB). While the period of two months will generally be applicable to companies for return of certificates relating to a security after registration of transfer of the security, in the case of listed company this period has been curtailed to one month by virtue of a provision in the listing agreement whereunder companies have agreed to return the certificates within one month of the date of lodgement for transfer [vide Clause 3(c) of the listing agreement].

Where the securities are dealt within a depository, the company is required to intimate the details of allotment of securities to depository immediately on allotment of such securities and every depository shall on receipt of intimation from a participant, register the transfer of securities in the name of the transferee. In case the beneficial owner or a transferee of any securities seeks to have custody of such securities, the depository shall inform the issuer accordingly.

Along with the Depositories Act, 1996 a new Sub-section (14) was added to Section 111 of the Companies Act, 1956 by which Section 111 was made applicable only to a private company. At the same time Section 22A of Securities Contracts (Regulation) Act, 1956 was repealed. Instead a new Section 111A was inserted in the Companies Act, 1956, which provided that:

1. The said section is applicable to a company other than a private company.
2. If a transfer of shares has been made wrongly, the Company Law Board*

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* now tribunal.
* now tribunal.
may order rectification of the register of members and debentureholders.

(3) The shares and debentures of a public company are freely transferable. Where a company refuses to register a transfer within two months of deposit of the instrument of transfer, the transferee may appeal to the Company Law Board* for directing the Company to register the transfer [This was added to Section 111A(2) by Depositories Related Laws (Amendment) Act, 1997 (5 of 1997)].

III. APPRAISAL OF SHARE TRANSFER WORK

The auditor is required to check the following aspects while conducting share transfer audit.

— Proper instrument should have been submitted to the company. Execution and delivery of share transfer form is an essential pre-requisite without which a company cannot register a transfer. The prescribed Form 7B should be duly endorsed by the ROC. In case of a company where shares are listed with OTC Exchange of India, the instrument of transfer should be in Form 7BB. The share transfer form may be lodged either by transferor or by transferee.

Verify whether the transfer falls within the purview of the following cases:

(i) share transferred by a director or nominee on behalf of another body corporate under Section 49(2) and (3);

(ii) shares transferred by a director or nominee on behalf of a corporation owned or controlled by the Central or State Government;

(iii) shares transferred by way of deposit as a security for repayment of any loan or advance if they are made with any of these: (a) State Bank of India or (b) any scheduled bank or (c) any banking company or (d) financial institution or (e) Central Government or (f) State Government (g) any corporation owned or controlled by the Central or State Government; or

(iv) trustees who have filed the declarations;

(v) transfer of debentures.

In the aforesaid, the instrument of transfer may not be in the prescribed form.

— Check whether transfer deed is duly stamped and executed both by transferor and transferee.

In the case of transfer of shares the stamp duty is uniform throughout the country. On every share transfer form, there shall be paid requisite Stamp Duty as per Indian Stamp Act, 1899 and the stamp duty payable on a share transfer is to be paid by affixing to transfer form special adhesive stamps bearing the words ‘Share Transfer’. In the absence of proof of payment of such consideration companies generally assume the market value of the shares on the date of execution of the transfer deed for the purpose of calculation of stamp duty. It should be noted that share transfer stamps of the value equivalent to the duty payable is to be affixed on the transfer deed and the stamps should be cancelled also before the transfer deed is lodged with the company. Strictly speaking, a company cannot accept a transfer deed for
registration unless share transfer stamps are affixed and the same are cancelled.

In the case of transfer of debentures or other securities the stamp duty payable on transfer thereof vary from State to State. The duty has to be paid at the time of execution. The duty so paid at the time of execution should, however, be not less than the duty payable in the State in which the Registered Office of the company is situate if the deed had been executed there. Please refer to the relevant provisions of the various State Stamp Acts.

If shares are held jointly by two or more persons, the instrument of transfer must be executed by all joint holders. Splitting of joint holding into individual shareholding will also require execution of a share transfer deed. In such a case, all joint holders shall sign a transfer deed as transferors and the respective individuals holders in whose favour splitting is to be made, shall sign as transferees.

— The signature of the transferor should tally with the specimen recorded with the company.

Where although the signatures are attested by Notary Public, the same do not tally or the signatures have not been properly attested, the companies are advised to satisfy themselves where there is doubt/apprehension about the genuineness of signatures by making a reference to the transferor.

However, a company cannot escape liability where attestation is done negligently. The signatures of the transferor in the share/debenture transfer form must be witnessed by other person, giving his name, signature and address.

— Where the instrument is executed by a person other than transferor or transferee named in instrument, on behalf of transferor or the transferee, the document authorising the executant to execute the instrument of transfer must be obtained by the company. If the transferor is a body corporate, it should be ensured that a Board resolution of the transferor has been passed and proper authority has been given by the Board of directors to the person signing as the transferor on behalf of the company.

— The share transfer form must be complete as regards other particulars i.e. name, address, occupation etc. of transferee.

— Share certificate or if no such certificate is in existence the letter of allotment of shares shall be delivered alongwith the instrument. Every instrument of transfer should be presented to the prescribed authority for dating before anything is filled in or signed by the transferor.

— Share transfer form must be presented in time limit for delivery of instrument, together with related certificates, in compliance with Section 108 of the Companies Act, 1956.

— If the transferee is a company then before registering the transfer it should be seen with reference to the Objects Clause of the Memorandum of Association of the company concerned whether it is one of the objects of the company to make investments in the securities of other companies and the investment is properly authorised by the Board of directors under Section 292
and, if applicable, under Section 372A of the Companies Act, 1956 and appropriate delegation has been given in favour of the person who has signed the transfer deed. In *Jagatjit Industries Ltd. and others v. Mohan Meakins Ltd. and others* (1991) 6 CLA 22 (CLB) companies need not indicate occupation in the relevant column of the transfer deed.

— Where the application is made by the transferee and relates to partly paid up shares, check whether the company has given due notice of application to the transferee and whether the transferee has raised objection, if any, within two weeks from the date of receipt of the said notice.

— If the signed transfer deed has been lost, the same stamp is affixed on the written application, in which case, the Board may, if it thinks fit, register the transfer on suitable terms of indemnity.

— Check whether any restriction, is/was at any time imposed on the transfer of shares, whether by the Articles or under any other law.

— Check whether the transferor and transferee are both entered as beneficial owners in the records of a depository in which case provisions of Section 108 do not apply.

— Check whether the transfer is in violation of provisions of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997.

— If the company is a listed company and Shares Transfer Agents are processing the company’s share transfer work, check whether they have followed the guidelines issued by various market intermediaries including general norms for processing of documents, norms for processing of transfers and norms for objection.

— Check whether all the work related to share registry in terms of both physical and electronic form is maintained by the company at a single point i.e. either in house by the company or by a SEBI registered Registrar and Transfer Agent.

— Check whether uniform guidelines prescribed by SEBI are followed by Registrars to an Issue (RTI)/Share Transfer Agents (STA) and companies for handling and processing of transfer documents

SEBI vide its circular No. 1 (2000-2001) dated May 09, 2001 has issued uniform guidelines to be followed by RTI/STA and companies. These guidelines have been divided into three parts:

(i) General norms for processing of documents.

(ii) Norms for processing of transfers.

(iii) Norms for objection.

Draft of the formats to be used have also been suggested in these guidelines.

All registered RTIs and STAs and companies listed on stock exchanges should mandatorily follow these guidelines and formats. These directions are issued pursuant to powers conferred on SEBI under Section 11B of SEBI Act, 1992.

In addition to the above aspects, the following aspects are to be kept in mind while effecting transfers.
(a) Appraisal of register of members/debenture holders

Check whether a company has properly maintained its register of members and register of debentureholders with respect to the following aspects:

— Whether the registers are maintained in the form prescribed under the Companies (Issue of Share Certificates) Rules, 1960 or as near thereto as circumstances admit.

— Whether the details of the transfers have been posted in the proper folios in the register of members. In case of transferee being a new member whether new folio has been allotted to him. In case after recording the transfer the holding of a member becomes nil whether the folio has been properly closed.

— Whether entries in the register are authenticated by the Secretary or any other person authorised by the Board.

— Whether in case of a company having more than 50 members an index of members is maintained.

— Whether every change in the register of members has been recorded in the index within 14 days.

— Whether the declarations received under Section 187C have been properly entered in the proper folio of the register of members.

(b) Processing of Dividends/Interest Warrants, considering share transfer

The paramount requirement in the processing of dividend/interest warrants is to determine the persons entitled to the dividend/interest as the case may be. For this purpose, under Section 154 of the Companies Act, 1956, companies are empowered to close the register of members/register of debentureholders by giving 7 days' clear notice by advertisement in some newspaper circulating in the district in which the registered office of the company is situate. In case of listed companies under the listing agreement companies are required to close the transfer books only once in a year with reference to the annual general meeting. For all other purposes the stock exchanges require fixation of record date. Before closing the transfer books or fixing the record date the concerned stock exchange should be given a notice at least 42 days in advance. In view of the above, in the case of listed companies while transfer books can be closed for the payment of dividend/final dividend, for all other purposes they can only fix a record date. Even though Section 154 of the Companies Act, 1956 is silent with regard to giving notice to members in regard to fixation of record date, it is necessary to publish notice in the same manner as is done for closure of register of members so as to enable the members/debentureholders to lodge the transfer deed in time for getting their entitlement.

All valid transfer deeds lodged with the company before the date of commencement of the closure of register of members/register of debentureholders or the record date should be given effect to and list of persons who are entitled for the dividend/interest as the case may be should be prepared.

Separate banking account should be opened for payment of dividend/interest, as the case may be. The dividend warrants/interest warrants should be got printed, prepared and duly signed. It should be kept ready for delivery. As soon as the
dividend is declared at the general meeting the dividend warrant should be posted. In the case of interest the same should be posted immediately after it becomes due for payment or even earlier but dating the interest warrant with the date on which the interest becomes due. In any case the dividend warrants should be sent to the persons entitled thereto within 30 days of the declaration of the dividend (Section 207).

Under the listing agreement listed companies are required to intimate the stock exchange at least 21 days in advance of the date on and from which date the dividend will be payable. Listed companies are also required to issue dividend warrants payable at par at such centres as may be agreed to between the stock exchange and the company. Even though listing agreement is silent about the interest warrant, the procedure set out above should equally apply for payment of interest on debentures which are listed on stock exchanges.

A Company Secretary in Practice should while appraising the processing of dividend and interest warrants keep the foregoing aspects in mind and ensure that they are scrupulously followed by companies.

(c) Despatch of Notice, Annual Report, Letter of Offer

Service of documents on members by a company is governed by Section 53 of the Companies Act, 1956 whereunder a document may be served by a company on any member either personally or by sending it by post to his registered address or if he has no registered address in India, to the address, if any, within India supplied by him to the company for giving of notices to him. It would be seen that strictly speaking, it is not necessary to send any document to a member under certificate of posting or by registered post. But if any member desires that a particular document should be sent to him under certificate of posting or by registered post or registered post acknowledgement due, he is required to deposit with the company a sum sufficient to defray the expenses in which event service of the said document will be deemed to be effected only if it is made in the manner desired by the member.

In view of the foregoing, unless a particular member has desired that notices etc. should be served on him under certificate of posting or by registered post or registered post acknowledgement due and has deposited the requisite amount therefor all documents including general meeting notice, annual report, etc. can be served on members by ordinary post. But in order to ensure a proof of service on the members in time generally companies send general meeting notices, annual reports, etc. under certificate of posting even though it is not a legal necessity.

(d) Signature Verification on Transfer Deed

Where it is found that the transferor’s signature on the transfer deed varies, a company is not bound to accept the deed even if it has been attested and the Ministry of Finance, Stock Exchange Division has advised companies that where there is a variation in the signature of the transferor, the company should send a notice to the transferor by registered post informing him of the receipt of the deed purportedly signed by him and that the company shall take action to register the transfer if the company does not receive any objection from the transferor within 21 days of the date of the said notice. This will help companies not to delay action in bona fide cases.
(e) Audit for reconciliation of the total admitted capital with both the depositories and the total issued and listed capital.

While conducting share transfer audit of a company which has both physical and demat shares, the auditor check the following aspects

(i) Whether the work related to share registry in terms of both physical and electronic is maintained at a single point i.e. either in-house by the company or by a SEBI registered R & T Agent.

(ii) Whether the company or the registrars and share transfer agents (RSTA) as the case may be are maintaining records of all the shares dematerialised, rematerialised and details of all securities declared to be eligible for dematerialisation in the depositories and

(iii) Whether dematerialisation of shares are confirmed / created only after an in-principle approval of the stock exchange / s where the shares are listed and the admission of the said share with the depositories have been granted.

(iv) Whether they shall have proper systems and procedures in place to verify that the securities tendered for dematerialisation have not been dematerialised earlier.

(v) whether they ascertain, reconcile daily and confirm to the depositories that the total number of shares held in NSDL, CDSL and in the physical form tally with the admitted, issued and listed capital of the issuer company; and

(vi) Whether they confirm that the dematerialisation requests have been processed within 21 days and shall also state the reasons for shares pending confirmation for more than 21 days from the date of request.

(vii) Whether Audit as specified by SEBI was undertaken by a qualified Chartered Accountant or a Company Secretary, for the purposes of reconciliation of the total admitted capital with both the depositories and the total issued and listed capital, ensuring the following aspects.

The total of the shares held in NSDL, CDSL and in the physical form tally with the issued / paid-up capital.

The Register of Members (RoM) is updated.

The dematerialisation requests have been confirmed within 21 days and state the shares pending confirmation for more than 21 days from the date of requests and reasons for delay.

The details of changes in share capital (due to rights, bonus, preferential issue, IPO, buyback, capital reduction, amalgamation, de-merger etc) during the quarter and certify in case of listed companies.

(viii) Whether in-principle approval for listing from all stock exchanges was obtained in respect of all further issues.

(ix) Whether the company has submitted the audit report on a quarterly basis to the stock exchange/s where they are listed.

(x) Whether there is any difference observed in the admitted, issued and listed capital.
(f) Safeguards to address the concerns of the Investors on Transfer of Securities in Dematerialized Mode

The concerns arising out of transfer of securities from the Beneficial Owner (BO) Accounts without proper authorization by the concerned investor have been brought to the notice of SEBI by some Investors’ Associations. Accordingly SEBI has decided to put in place the following safeguards to address the concerns of the investors on electronic transfer:

(a) The depositories shall give more emphasis on investor education particularly with regard to careful preservation of Delivery Instruction Slip (DIS) by the BOs. The Depositories may advise the BOs not to leave “blank or signed” DIS with the Depository Participants (DPs) or any other person/entity.

(b) The DPs shall not accept pre-signed DIS with blank columns from the BO(s).

(c) The DPs shall issue only one DIS booklet containing not more than 20 slips for individual account holders and not more than 100 slips for non-individual account holders, at a time.

(d) If the DIS booklet is lost/stolen/not traceable by the BO, the same must be intimated to the DP immediately by the BO in writing. On receipt of such intimation, the DP shall cancel the unused DIS of the said booklet.

(e) The DPs can issue subsequent DIS booklet to a BO only after the BO has used not less than 75 per cent of the slips contained in the previous DIS booklet. The DP shall also ensure that a new DIS booklet is issued only on the strength of the DIS instruction request slip (contained in the previous booklet) duly complete in all respects, unless the request for fresh booklet is due to loss, etc., as referred to in clause (d) above.

(f) The DPs shall not issue more than 10 loose DIS to one account-holder in a financial year (April to March). The loose DIS can be issued only if the BO(s) come in person and sign the loose DIS in the presence of an authorised DP official.

(g) The DPs shall put in place appropriate checks and balances with regard to verification of signatures of the BOs while processing the DIS.

(h) The DPs shall cross check with the BOs under exceptional circumstances before acting upon the DIS.

(i) The DPs shall mandatorily verify with a BO before acting upon the DIS, in case of an account which remained inactive i.e., where no debit transaction had taken place for a continuous period of 6 months, whenever all the ISIN balances in that account (irrespective of the number of ISINs) are transferred at a time. However, in case of active accounts, such verification may be made mandatory only if the BO account has 5 or more ISINs and all such ISIN balances are transferred at a time. The authorized official of the DP verifying such transactions with the BO, shall record the details of the process, date, time, etc., of the verification on the instruction slip under his signature.

IV. CERTIFICATION
Companies are not required to get share transfer audit done but companies whether listed or not are required to file within two months of the holding of the Annual General Meeting a list of members, debentureholders etc. once in six years with the Registrar of Companies alongwith the Annual Return. In the case of listed companies the Annual Return is required to be signed by a secretary in whole-time practice. Therefore, before signing the Annual Return as above Company Secretary in practice is required to examine the transfer records to satisfy himself that the transfers have been properly registered and in case any request for registration of transfer has been refused, the company concerned has complied with the requirements of section 108 and section 111A of the Companies Act. Of course, it will not be practicable to verify each and every transfer lodged with the company in case of medium sized and big companies. Therefore, the Company Secretary in practice can make a test check or a random check of the transfers. He should further invariably go through the agenda papers and minutes of the meeting of the Board of directors or Committee of directors in which matters relating to the registration of transfers or refusal to registration of transfers have been complied with. It may be added that the legal position has been broadly outlined above, but the Company Secretary in Practice is required to keep himself up-to-date on the law relating to share transfer and confirm compliance of the same while examining the transfers.

Also, in pursuance of Clause 47(a) of the Listing Agreement, a listed company has to appoint a Company Secretary as a compliance officer who will be responsible for monitoring the share transfer process and report to the company’s board in each meeting. As a compliance officer, the company secretary is required to directly liaise with the authorities such as SEBI, Stock Exchanges, ROC etc. and investors with respect to implementation of various clauses, rules, regulations and other directives of such authorities and investor service and complaints related matters.

Therefore, it is imperative for company secretaries to be conversant with the legal and procedural aspects of transfer of shares/debentures.

(a) Certification of Securities Transfers in Compliance with the Listing agreement with Stock Exchanges

In furtherance of objective of protecting the interests of investors in securities, SEBI by its Circular Letter No. SMD/POLICY/CIR/06/98 dated February 10, 1998 advised all Stock Exchanges to amend the listing agreement so as to improve stipulations to provide for speedy registration of securities and monitoring by the Board of Directors of listed companies and by the Stock Exchanges and by SEBI. It may be seen therefrom that one of the additional requirement suggested is that a listed company should insist on the RTA to produce to it a certificate from a Practising Company Secretary that all transfers have been completed within the stipulated time. In compliance of the instructions of SEBI, the various Stock Exchanges have amended their listing agreement providing for the various additional requirements including the requirement that a listed company should procure and produce from a Practising Company Secretary a certificate that all transfers have been completed within the stipulated time. Of course, each exchange has given its own serial number to the clause providing for this requirement. However, the Stock Exchange, Mumbai has gone ahead and has provided that such a certificate should be procured not only in respect of issue of certificates lodged for transfers but also in respect of issue of certificates on sub-division, consideration, renewal, exchange or endorsement of
calls/allotment monies. In addition, while SEBI has suggested certification in respect of RTA (which includes inhouse securities transfer facility where at any time the total number of the holders of securities exceed one lakh), the Mumbai Stock Exchange has stipulated that in respect of all inhouse securities transfer facility also, certification should be procured from a Practising Company Secretary and shall be made available to the exchange within 24 hours of the receipt of the certificate by the company. Also while SEBI has stipulated that the certificate should certify that all transfers have been completed in time, the Stock Exchange at Mumbai has stipulated that the relative certificates have been issued within one month of the date of lodgment for transfer, sub-division etc. These additional requirements of the Stock Exchange, Mumbai have also been adopted by the various other stock exchanges. The term ‘issue’ which had been used in the listing agreement has not been defined in the listing agreement or any Rule or Regulation framed under the Securities Contracts (Regulation) Act, 1956. In Section 113 of the Companies Act, 1956, the word, in connection with the transfer of shares, used is ‘deliver’. The word ‘issue’ is a word of wide import but keeping in view the objective of the amendment it should be given the meaning which will serve the purpose for which the amendment has been made. Keeping this in view, the word ‘issued’ should appropriately mean ‘sent out’. Accordingly, in order to comply with the requirement a listed company should despatch the certificate within one month of the lodgement for transfer. Further the requirement of certification is confined to transfer (i.e. by agreement or by action of parties) and not to transmission of securities (i.e. by operation of law). In the latter case it is possible that in a given situation it may not always be possible to keep up to the prescribed period of one month for the despatch of certificates. Hence, the certification need not cover transmission cases. However, while examining the transfer for the purpose of certification a Company Secretary in Practice can alert the companies wherever a transmission has been unduly delayed. Alternatively, it may be ensured that the certificates are despatched within one month of the person lodging the papers for transmission after complying with the requirements stipulated by the company. The certification of securities transfer and other incidental matters as above stipulated by the exchanges in the country and the Stock Exchanges, Mumbai in particular, has opened up scope and area of practice for practising members.

(b) Salient Provisions in the listing agreement

Clauses 3(c) and 6 of the Listing Agreement mainly deal with the subject matter of the certification.

Under sub-clause (c) of clause 3, a listed company is required to issue certificates within one month of the date of lodgement for transfer, sub-division, consolidation, renewal, exchange or endorsement of calls/allotment monies. Thus, with regard to securities transferred generally, a listed company is required to transfer and issue the relative certificate for securities within a period of one month from the date of lodgement of transfer.

Also clause 6 of listing agreement provides that the issuer will, if so required by the exchange, certify transfers against letters of allotment, certificates and balance receipts and in that event the company will promptly make on transfers an endorsement to the following effects:
Apart from this various other clauses like Clause 7, 8, 10, 11, 12, 12A, 13, 14, 15, 16, 17, 21, 23, 34, 47 in the Listing Agreement cover the gamut of Share Transfer.

Keeping the aforesaid provisions in the listing agreement in view before certifying that a listed company has complied with these requirements, a Company Secretary should normally be required to verify in respect of each transfer lodged with the company, whether the relative certificate has been despatched after making endorsement of transfers within the stipulated time. While this is the general rule, it may not be always physically possible for a Company Secretary to verify each and every transfer deed, particularly, in the case of a company whose shares are frequently traded and the volume of transfers is large. In such cases, he can, on going through the systems and procedures in place with regard to transfers of securities, consolidation, renewal or exchange of securities and for endorsement of calls assess the extent to which he has to verify the facts for the purpose of this certification, e.g. if a Practising Company Secretary is convinced of the adequacy of the systems and procedures, he may decide to have a random or test check and decide to issue a certificate based on such a check. However, it should be borne in mind at the time of a random or test check if the Practising Company Secretary comes across considerable deficiencies in this regard, he should undertake complete check of all transfers. In any case no hard and fast rule can be laid down as regards the extent to which this check should be conducted. This will depend largely upon the position existing in the company and the judgement of the Practising Company Secretary concerned, even though he is required to certify about the completeness of transfer and despatch of certificates within the stipulated time.

The examination should not be confined only to duly completed transfer deeds lodged with the company but it should also include transfer lodged with the company which are deficient and are retained by the company after making a reference or returned to the lodger for making good the deficiency. Keeping in view the purpose for which the certification has been stipulated, it is but proper that the verification should cover all transfers lodged with the company whether they are fit for transfer or not. Transfer in respect of deficient transfer, return or reference to the lodger should also be done within a period of one month from the date of lodgement of transfer deeds. There should not be any delay in this regard.

(c) Periodicity of Certification

While the letter from SEBI to the Stock Exchanges makes no reference to the periodicity of certification, the Mumbai Stock Exchange has stipulated that such a certification should be given within one month of the close of each half of the financial year. Further the exchanges at Mumbai, Pune, Calcutta and Uttar Pradesh (Kanpur) has stipulated that the certificate given by the Practising Company Secretary should be sent to it within 24 hours of its receipt by the listed company. In view of the fact
that the financial year varies from company to company, the period to which such a certificate has to be given may also vary. Accordingly, this certificate in relation to securities quoted on the Stock Exchange should be in relation to each half of the financial year of the company. As regards the securities quoted on other stock exchanges this certificate can be given with reference to each financial year, or with reference to each book closing or record date as the case may be and the same should be made available within one month of the period to which it relates. It should be noted that the amendment to the listing agreement stipulated by Exchanges other than the Mumbai, Pune and Calcutta Stock Exchanges do not specify that this certificate should be made available to the exchange concerned. However, it would be prudent for a listed company to send a copy of the certificate as and when it is made available to it by the RTA.

(d) Extent of Examination

For the purpose of the certification, it would not be necessary for a Company Secretary to examine whether the transfer deed has been properly registered by the listed company, it is enough if he verifies that the transfer deed in relation to securities lodged with the listed company has been dealt with by it either by despatching the relative securities certificate duly endorsed or the lodger has been informed of the deficiencies where a transfer is not registered, within the period of one month from the date of lodgement. Therefore, the Company Secretary should largely confine himself to the examination of only those books, records and papers relating to receipt of transfer documents and despatch of certificates or issue of letters pointing out the deficiency, return of transfer instruments as the case may be. Almost all the information for the purpose will be available in securities transfer receipt register being maintained by the listed companies. If such a register is not maintained by the company, the Company Secretary may advise the company to maintain such a register either manually or by electronic process so that future certifications will be facilitated.

The Institute has suggested the format of the certificate, a copy of which is reproduced at Annexure A. This format has been devised to guide the Practising Company Secretaries concerned as to what the certificate should contain. A Practising Company Secretary is free to amend the same or adopt the same depending upon the specific circumstances in relation to a company.

As regards return of transfer deeds the certificate need not contain individual details in regard to transfers returned or retained for making good deficiencies therein. It would be enough if all such transfers are grouped deficiency-wise and listed in an Annexure to the return. The deficiencies largely will fall under any one or more of the following:

1. Deficiency in stamping
2. Transfer signature differs
3. Restraint order by competent authority on registration of transfer
4. Non-approval of transfers by a proper Government authority
5. Transfers infringing the provisions of laws, rules or regulations
6. Various securities are sought to be transferred through a single instrument
7. Others (specify).
It is possible that all completed transfers received up to the date of the certificate have not been given effect to and the certificates despatched before that date. The certificate should, therefore, also mention the number of transfers pending for registration.

The Practising Company Secretary should in respect of share certificates issued on consolidation, sub-division or duplicate share certificates examine the records maintained by the company under the Companies (issue of Share Certificates) Rules, 1969 before issuing the certification.

ANNEXURE A

Format of Certificate to be given by a Practising Company Secretary

I/We* have examined the relevant books and records of ______ Ltd. (Company) produced before me/us for the purpose of issuing the Certificate under sub-clause____ of clause____ of the Listing Agreement with the _____ Stock Exchange and based on my/our* such examination as well as information and explanations furnished to me/us* which to the best of my/our* knowledge and belief were necessary for the purposes of my/our* certification. I/We* hereby certify that in my/our* opinion and according to the best of my/our* information and belief the company has, in relation to the half year (year) ended____ delivered all certificates within the period stipulated under the Listing Agreement from the date of lodgement for transfer, sub-division consolidation, renewal, exchange or endorsement of calls/allotment monies.

*(Strike out whichever is not applicable).

LESSON ROUND-UP

Registration of transfer of shares, debentures and other securities is one of the main and important works of a Company Secretary in a company.

All companies listed on stock exchanges are required to do the processing of share transfers and effect transfers in accordance with the provisions of the Companies Act, 1956, listing agreement and the guidelines issued by SEBI.

Work related to share registry in terms of both physical and electronic should be maintained at a single point i.e. either in-house by the company or by a SEBI registered R & T Agent.

As per the listing agreement, a listed company should insist on the RTA to produce to it a certificate from a Practicing Company Secretary that all transfers have been completed within the stipulated time.

While effecting electronic transfers, DPs are advised to take safeguards on aspects such as delivery instruction slip etc.

SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation)

1. State the areas which need to be verified for appraisal of share transfer work.

2. Is it necessary for a company to get a share transfer audit done? State how
3. Write a brief note on Audit for reconciliation of total admitted capital with both the depositories and the total issued and listed capital.

4. What are the safe guards to be taken in case of electronic transfer.
LEARNING OBJECTIVES

- The objective of this study lesson is to enable the students to understand
  - Concept and need of compliance certificate
  - Various provisions of Companies (Compliance Certificate) Rules, 2001
  - Check list for compliance certificate
  - Various e-forms to be filed with the Registrar of Companies

CONCEPT AND NEED

The successive Annual Reports on the Working and Administration of the Companies Act, 1956 reveal that a large number of documents are returned for rectification of defects and also remain pending for being taken on record. It cannot be denied that in case of documents returned for rectification, a large number of errors or omissions arise on account of mis-interpretation or ignorance of the provisions of law. Further, the Ministry of Corporate Affairs institutes every year, a large number of prosecutions against the companies and their officers in default for contravention of various provisions of the Companies Act. Most of the companies against which prosecutions are instituted are private limited companies or small public limited companies which do not have the benefit of expert professional services of qualified Company Secretaries.

Thus, it is a well established fact that smaller companies fall prey to violations of the provisions of the Companies Act in the absence of professional support as compared to companies which have employed a qualified Company Secretary.

The Companies (Amendment) Act, 2000 had inserted a proviso to Sub-section (1) of Section 383A of the Companies Act which provides that every company having such paid-up share capital as may be prescribed* shall have a whole-time secretary and where the Board of Directors of such company comprises only two directors, neither of them shall be the secretary of the company. However, every company not required to employ a whole-time secretary under Sub-section (1) and having a paid-up share capital of ten lakh rupees or more shall file with the Registrar a certificate from a secretary in whole-time practice in such form and within such time and subject to such conditions, as may be prescribed, as to whether the company has complied with all the provisions of this Act, and a copy of such certificate shall be attached with Board's report, referred to in Section 217.

A company with its registered office and corporate office and works situated in towns with a population of less than one lakh in accordance with Census of India 2001 Report and having a paid-up share capital of rupees two crores or more but less than rupees five crores, may appoint any individual, who possess any one or more of the qualifications specified in clause (i) to (x) of sub-rule (4) of Rule 4 of Companies (Appointment and Qualifications of Secretary) Rules, 1988 as its whole-time

* at present, two crores.
secretary to perform the duties as such under the Companies Act, 1956 (1 of 1956).

Also if a company having a paid-up share capital of rupees two crores or more but less than rupees five crores shifts either its registered office or corporate office or works from towns with a population of less than one lakh in accordance with Census of India 2001 Report, it shall appoint a person as a whole-time Secretary under sub-rule (1) of Rule 2.

Accordingly, every company having a paid-up share capital of rupees ten lakh or more but less than rupees two crores is required to file with the Registrar of Companies (ROC), a Compliance Certificate obtained from a secretary in whole-time practice and also attach a copy of the certificate with a report of the Board of Directors of the Company.

However, the Ministry of Corporate Affairs in its Circular, DCA Circular No. 35/2003 dated 11.12.2003 clarified that a company having paid up capital less than Rs. 2 crore (but more than Rs. 10 lakh) is not required to submit secretarial compliance certificate, if the company has appointed a whole time qualified company secretary in employment.

Compliance Certificate is, therefore, salutary as it creates an awareness among companies to comply with the provisions of the Companies Act and also provides a mechanism for self regulation by companies.

Compliance Certificate not only acts as an effective mechanism to ensure that the legal and procedural requirements under the Companies Act are duly complied with but also instills professional discipline in the working of the company besides building up the necessary confidence in the state of affairs of the company. It will relieve the company and its directors including the nominee directors from the consequences of unintended non-compliance of the provisions of the Companies Act. It will further curb the tendency on the part of the smaller companies to short circuit the procedural requirements which primarily occur due to ignorance or lack of professional support. It will act as a pre-emptive check to monitor compliance with the requirements of the Companies Act and the Rules made thereunder.

The Company Secretary, while undertaking the work of issuing Compliance Certificate will act as a friend and guide to the management of companies. There is also a need to educate the management of small companies and to instill professionalism in their management so that these companies appreciate their contribution. Only a positive and helpful approach can build the necessary confidence. If there have been technical non-compliances, the approach should be to guide and advise the company to make good the deficiencies by maintaining proper records, filing the requisite returns or seeking compounding of offences.

**THE COMPANIES (COMPLIANCE CERTIFICATE) RULES, 2001**

In terms of the newly inserted proviso to Sub-section (1) of Section 383A, the Central Government has prescribed the Companies (Compliance Certificate) Rules, 2001 (hereinafter called the rules) for issue of Compliance Certificate by a Practising Company Secretary.

The Rules have come into force w.e.f. February 1, 2001 i.e. the date of their
publication in the Official Gazette.

According to Sub-rule (1) of Rule 3, every company not required to employ a whole-time secretary under Sub-section (1) of Section 383A of the Act and having a paid-up share capital of ten lakh rupees or more shall obtain a certificate from a Practising Company Secretary.

SCOPE OF COMPLIANCE CERTIFICATE

The scope of Compliance Certificate would comprise of certification of the compliance of various requirements under the Companies Act and the Rules thereunder. The Practising Company Secretary should certify compliance only in respect of matters specified in the Form prescribed under the Rules and where any matter is not applicable, he should specify accordingly.

Sub-rule (2) of Rule 3 specifies that the Compliance Certificate shall be in Form appended to the Rules or as near thereto as circumstances admit. Certain amount of flexibility in the Form has, therefore, been provided which means that if any information required to be given in the certificate does not fit into the format, necessary modifications may be made in the format by the Practising Company Secretary.

At the time of issue of the first Compliance Certificate, the Practising Company Secretary should verify the registers and records maintained by the company from the first day of the financial year except where there are reasons for Practising Company Secretary to verify the records for the earlier years. Such occasions may arise in respect of maintenance of registers, retirement of directors by rotation, issue of share certificate when the allotments were made in the earlier years, payment of managerial remuneration, etc.

Period of Certification

Sub-rule (2) of Rule 3 provides that the Compliance Certificate shall relate to the period pertaining to the financial year of the company. The Companies (Amendment) Act, 2000 has come into force w.e.f. 13th December, 2000 and the Companies (Compliance Certificate) Rules, 2001 have come into force w.e.f. 1st February, 2001. Accordingly every company to which these Rules are applicable is required to obtain a Compliance Certificate from a Practising Company Secretary for the financial year in respect of which Board’s report is signed on or after 1st February, 2001.

Filing of Compliance Certificate

Every company to which these Rules apply is required to file with the ROC the Compliance Certificate within thirty days from the date on which its annual general meeting is held.

Where the annual general meeting of such company for any year has not been held, such certificate is required to be filed with the ROC within thirty days from the latest day on or before which that meeting should have been held in accordance with the provisions of the Companies Act.
In case the annual general meeting is held and adjourned, the Compliance Certificate should be filed with the ROC within thirty days from the date on which such adjourned meeting was held provided such adjourned meeting is held within the statutory limit.

**Right of Practising Company secretary to Access Records**

Sub-rule (3) of Rule 3 provides that the Practising Company Secretary for the purpose of issue of Compliance Certificate shall have right to access at all times to the registers, books, papers, documents and records of the company whether kept in pursuance of the Act or any other Act or otherwise and whether kept at the registered office of the company or elsewhere and shall be entitled to require from the officers or agents of the company, such information and explanations as the Practising Company Secretary may think necessary for the purpose of such certificate.

**Attachment of Compliance Certificate with Board’s Report**

Proviso to Sub-section (1) of Section 383A of the Act requires that the Compliance Certificate shall be attached with the Board’s report referred to in Section 217. It is, therefore, necessary for the company to attach a copy of the Compliance Certificate with the Board’s report while forwarding the same to members and others under Section 219 of the Act.

Further it would also be desirable for the Board to give full information and explanation in its report to the members under Section 217 of the Act on every reservation, qualification or adverse remarks contained in the Compliance Certificate.

**Laying of the Compliance Certificate at the Annual General Meeting**

Sub-rule (4) of Rule 3 requires the Compliance Certificate to be laid by the company in its annual general meeting. As a good secretarial practice, the certificate should be read at the meeting and also made available to the members for inspection.

**Penalty for non-compliance**

Where a company fails to comply with the requirement of filing the Compliance Certificate with the Registrar of Companies or attaching the copy of such certificate with Board’s report, in terms of Sub-section (1A) of Section 383A the company and every officer of the company who is in default shall be punishable with fine which may extend to Rs. 500 for every day during which the default continues.

**PRACTISING COMPANY SECRETARY: MODE AND PERIOD OF APPOINTMENT**

As the Compliance Certificate is required to be addressed to the members of the company, it would be in the fitness of things that the appointing authority is the members to whom this certificate is addressed. It is advisable that the Practising Company Secretary is appointed by the members in the annual general meeting of the company. Such appointment shall be from the conclusion of that annual general meeting until the conclusion of the next annual general meeting. It is also recommended that the first appointment of the Practising Company Secretary may be made by the Board of Directors to hold office until the conclusion of the annual general meeting held after such appointment.
The Board may fill any casual vacancy in the office of Practising Company Secretary to hold office until the conclusion of the next annual general meeting. However, if such a vacancy is caused by the resignation of Practising Company Secretary, it is advisable that the vacancy is filled up by the company in general meeting.

**Disqualifications of secretary in whole-time practice**

With a view to ensure that Practising Company Secretary shows utmost integrity and independence of judgement in the performance of his duties, a person referred to in Sub-section (3) or Sub-section (4) of Section 226 of the Act, should not be eligible for appointment or reappointment for giving Compliance Certificate to a company.

Accordingly, the following persons shall not be qualified for appointment as Practising Company Secretary of a company:

(a) a body corporate;
(b) an officer or employee of the company;
(c) a person who is a partner, or who is in the employment, an officer or employee of the company;
(d) a person who is indebted to the company for an amount exceeding one thousand rupees, or who has given any guarantee or provided any security in connection with the indebtedness of any third person to the company for an amount exceeding one thousand rupees;
(e) a person holding any security of that company which carries voting rights.

However, any securities held by such person as nominee or trustee for any third person and in which the holder has no beneficial interest shall be excluded from such disqualification.

Further, if a person is not qualified for appointment as Practising Company Secretary of a company for reasons stated above, then he is also disqualified for appointment as Practising Company Secretary of any other body corporate which is that company’s subsidiary or holding company or a subsidiary of that company’s holding company, or would be so disqualified if the body corporate were a company.

If a Practising Company Secretary becomes subject, after his appointment, to any of the disqualifications specified above, he shall be deemed to have vacated his office.

**Communication to earlier incumbent**

In view of the provisions of clauses (8) and (11) of Part I of the First Schedule to the Company Secretaries Act, 1980, it is recommended that whenever a new incumbent is assigned the compliance certification work, he should communicate his appointment to the earlier incumbent by registered post.

**Methodology for carrying out verification for certification**

It would be advisable that the Practising Company Secretary requests the company for access to various documents and books including the Memorandum and
Articles of Association of the company, Annual Reports of the last two to three years, various statutory and other registers including the Minutes Books, copies of forms and returns filed with the ROC etc. which he considers essential for the purposes of laying down the certification programme.

Practising Company Secretary should verify all the available records. However, depending on the facts and circumstances he may obtain a letter of representation from the company in respect of matters where verification by Practising Company Secretary may not be practicable, for example matters like—

(i) dis-qualification of directors
(ii) show cause notices received
(iii) persons and concerns in which directors are interested.

Certification with qualification

As specified in the Form, the qualification, reservation or adverse remarks, if any, may be stated by the Practising Company Secretary at the relevant places.

If the scope of work required to be performed, is restricted on account of limitations imposed by the client or on account of circumstantial limitations (like certain books or papers being in custody of another person or Government Authority) the certificate may be qualified as such.

Practising Company Secretary shall have due regard to the circulars and/or clarifications issued by the Ministry of Corporate Affairs from time to time. It is recommended that a specific reference of such circulars at the relevant places in the certificate may be made, wherever necessary.

Penalty for false Compliance Certificate

Section 628 deals with penalty for false statements. According to said Section, if in any return, report, certificate, balance sheet, prospectus, statement or other document, required by or for the purpose of any of the provisions of the Act, any person makes a statement

(a) which is false in any material particular, knowing it to be false, or
(b) which omits any material fact, knowing it to be material;

he shall, except as otherwise expressly provided in the Act, be punishable with imprisonment for a term which may extend to two years and shall also be liable to fine.

In view of this, a Practising Company Secretary will be attracting the penal provisions of Section 628, for any false statement in any material particular or omission of any material fact in the Compliance Certificate. However, a person will be penalised under Section 628 in case he makes a statement, which is false in any material particular, knowing it to be false, or which omits any material fact knowing it to be material.

PROFESSIONAL RESPONSIBILITY

While the newly inserted provision has opened up the much awaited significant area of practice for company secretaries, it equally casts onerous responsibility on
them and poses a greater challenge whereby they have to justify fully the faith and confidence reposed by the Government and trade and industry and measure up to their expectations. Company Secretaries must take adequate care while issuing Compliance Certificate. It is based on this certificate that confidence of the company, Government and trade and industry will build-up vis-a-vis our profession. Any failure or lapse on the part of a Practising Company Secretary in issuing a Compliance Certificate may not only attract penalty for false statement under Section 628 and disciplinary action for professional or other misconduct under the provisions of the Company Secretaries Act, 1980 but also make him liable for any injury caused to any person due to his negligence in issuing the Compliance Certificate. Therefore, it becomes imperative for the Practising Company Secretary that he exercises great care and caution while issuing the Compliance Certificate and also adheres to the highest standards of professional ethics and excellence in providing his services.

Fees for Compliance Certification

The scale of fees for compliance certification may be based on criteria, like paid-up share capital, number of shareholders and debenture holders, nature and standard of secretarial practices prevalent in the company, man-hours involved etc. However, the minimum fee for certification shall ordinarily not be less than Rs. 5,000 for a financial year.

As the scale of fees for compliance certification may be based on criteria, like paid-up share capital, number of shareholders and debenture holders, nature and standard of secretarial practices prevalent in the company, man-hours involved etc. the minimum fee for certification shall ordinarily not be less than the following amount(s) for a financial year:

<table>
<thead>
<tr>
<th>Paid-up Share Capital of the Company</th>
<th>Amount of Fee (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than Rs.50,00,000</td>
<td>5,000</td>
</tr>
<tr>
<td>Rs.50,00,000 but less than Rs.100,00,000</td>
<td>7,500</td>
</tr>
<tr>
<td>Rs.100,00,000 and above</td>
<td>10,000</td>
</tr>
</tbody>
</table>

CEILING ON NUMBER OF COMPANIES TO WHICH A PCS CAN ISSUE COMPLIANCE CERTIFICATE

In exercise of the powers conferred by Clause (1) of Part II of the Second Schedule to the Company Secretaries Act, 1980 (56 of 1980), as amended by the Company Secretaries (Amendment) Act, 2006, the Council of the Institute of Company Secretaries of India has specified that:

A member of the Institute in practice who is entitled—

(i) to issue compliance certificate to the proviso to Sub-section (1) of Section 383A of the Companies Act, 1956 (1 of 1956); and/or

(ii) to sign an Annual Return pursuant to the proviso to Sub-section (1) of Section 161 of the Companies Act, 1956 (1 of 1956), shall be deemed to be
guilty of professional misconduct if he—
— issues compliance certificates; and/or
— signs Annual Return

for more than eighty companies in aggregate, in a calendar year.

Provided, however, that in the case of a firm of Company Secretaries, the ceiling of eighty companies aforesaid would apply to each partner therein who is entitled to (i) sign the compliance certificate in terms of the proviso to Sub-section (1) of Section 383A of the Companies Act, 1956; (ii) sign Annual Return in terms of the proviso to Sub-section (1) of Section 161 of the Companies Act, 1956.

FORMAT OF COMPLIANCE CERTIFICATE
[vide Notification G.S.R. 52(E) dated 31.1.3001]

FORM
[See Rule 3]

Compliance Certificate

To,
The Members
__________________(Name of the company)

I/We have examined the registers, records, books and papers of___________________ Limited (the Company) as required to be maintained under the Companies Act, 1956, (the Act) and the rules made thereunder and also the provisions contained in the Memorandum and Articles of Association of the Company for the financial year ended on 31st March, 20__. In my/our opinion and to the best of my/our information and according to the examinations carried out by me/us and explanations furnished to me/us by the company, its officers and agents, I/we certify that in respect of the aforesaid financial year:

1. the company has kept and maintained all registers as stated in Annexure ‘A’ to this certificate, as per the provisions and the rules made thereunder and all entries therein have been duly recorded.

2. the company has duly filed the forms and returns as stated in Annexure ‘B’ to this certificate, with the Registrar of Companies, Regional Director, Central Government, Company Law Board or other authorities within the time prescribed under the Act and the rules made thereunder.

3. the company being private limited company has the minimum prescribed paid-up capital and its maximum number of members during the said financial year was ________ excluding its present and past employees and the company during the year under scrutiny:

   (i) has not invited public to subscribe for its shares or debentures; and
   (ii) has not invited or accepted any deposits from persons other than its members, directors or their relatives.
4. the Board of Directors duly met _______ times on ________(dates) in respect of which meetings proper notices were given and the proceedings were properly recorded and signed including the circular resolutions passed in the Minutes Book maintained for the purpose.

5. the company closed its Register of Members, and/or Debentureholders from _______ to _______ and necessary compliance of Section 154 of the Act has been made.

6. the annual general meeting for the financial year ended on _______ was held on _______ after giving due notice to the members of the company and the resolutions passed thereat were duly recorded in Minutes Book maintained for the purpose.

7. _______ extraordinary meeting(s) was/were held during the financial year after giving due notice to the members of the company and the resolutions passed thereat were duly recorded in the Minutes Book maintained for the purpose.

8. the company has advanced loan amounting to Rs._________ to its directors and/or persons or firms or companies referred in the Section 295 of the Act after complying with the provisions of the Act.

9. the company has duly complied with the provisions of Section 297 of the Act in respect of contracts specified in that section.

10. the company has made necessary entries in the register maintained under Section 301 of the Act.

11. the company has obtained necessary approvals from the Board of Directors, members and previous approval of the Central Government pursuant to Section 314 of the Act wherever applicable.

12. the Board of Directors or duly constituted Committee of Directors has approved the issue of duplicate share certificates.

13. the Company has:

(i) delivered all the certificates on allotment of securities and on lodgment thereof for transfer/transmission or any other purpose in accordance with the provisions of the Act;

(ii) deposited the amount of dividend declared including interim dividend in a separate bank account on _______ which is within five days from the date of declaration of such dividend;

(iii) paid/posted warrants for dividends to all the members within a period of 30 (Thirty) days from the date of declaration and that all unclaimed/unpaid dividend has been transferred to Unpaid Dividend Account of the Company with _________ Bank on____________;

(iv) transferred the amounts in unpaid dividend account, application money due for refund, matured deposits, matured debentures and the interest accrued thereon which have remained unclaimed or unpaid for a period of seven years to Investor Education and Protection Fund;

(v) duly complied with the requirements of Section 217 of the Act.
14. the Board of Directors of the company is duly constituted and the appointment of directors, additional directors, alternate directors and directors to fill casual vacancies have been duly made.

15. the appointment of Managing Director/Whole-time Director/Manager has been made in compliance with the provisions of Section 269 read with Schedule XIII to the Act and approval of the Central Government has been obtained in respect of appointment of__________________________ not being in terms of Schedule XIII.

16. the appointment of sole-selling agents was made in compliance of the provisions of the Act.

17. the company has obtained all necessary approvals of the Central Government, Company Law Board, Regional Director, Registrar or such other authorities as may be prescribed under the various provisions of the Act.

18. the directors have disclosed their interest in other firms/companies to the Board of Directors pursuant to the provisions of the Act and the rules made thereunder.

19. the company has issued__________shares/debentures/other securities during the financial year and complied with the provisions of the Act.

20. the company has bought back__________shares during the financial year ending ______ after complying with the provisions of the Act.

21. the company has redeemed__________preference shares/debentures during the year after complying with the provisions of the Act.

22. the company wherever necessary has kept in abeyance rights to dividend, rights shares and bonus shares pending registration of transfer of shares in compliance with the provisions of the Act.

23. the company has complied with the provisions of Sections 58A and 58AA read with Companies (Acceptance of Deposit) Rules, 1975/the applicable directions issued by the Reserve Bank of India/any other authority in respect of deposits accepted including unsecured loans taken, amounting to Rs._____________raised by the company during the year and the company has filed the copy of Advertisement/Statement in lieu of Advertisement/necessary particulars as required with the Registrar of Companies __________ on _______________. The company has also filed return of deposit with the Registrar of Companies/Reserve Bank of India/other authorities.

24. the amount borrowed by the Company from directors, members, public, financial institutions, banks and others during the financial year ending____is/are within the borrowing limits of the company and that necessary resolutions as per Section 293(1)(d) of the Act have been passed in duly convened annual/extraordinary general meeting.

25. the company has made loans and investments, or given guarantees or provided securities to other bodies corporate in compliance with the provisions of the Act and has made necessary entries in the register kept for the purpose.
26. the company has altered the provisions of the memorandum with respect to situation of the company's registered office from one State to another during the year under scrutiny after complying with the provisions of the Act.

27. the company has altered the provisions of the memorandum with respect to the objects of the company during the year under scrutiny and complied with provisions of the Act.

28. the company has altered the provisions of the memorandum with respect to name of the company during the year under scrutiny and complied with the provisions of the Act.

29. the company has altered the provisions of the memorandum with respect to share capital of the company during the year under scrutiny and complied with the provisions of the Act.

30. the company has altered its articles of association after obtaining approval of members in the general meeting held on ________ and the amendments to the articles of association have been duly registered with the Registrar of Companies.

31. a list of prosecution initiated against or show cause notices received by the company for alleged offences under the Act and also the fines and penalties or any other punishment imposed on the company in such cases is attached.

32. the company has received Rs. ________ as security from its employees during the year under certification and the same has been deposited as per provisions of Section 417(1) of the Act.

33. the company has deposited both employee's and employer's contribution to Provident Fund with prescribed authorities pursuant to Section 418 of the Act.

**Note:** The qualification, reservation or adverse remarks, if any, may be stated at the relevant place(s).

Place:            Signature:
Date:            Name of Company Secretary:
C.P. No.:

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**Annexure A**

Registers as maintained by the Company
1. __________________ u/s ______________
2. __________________ u/s ______________
3. __________________ u/s ______________

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**Annexure B**

Forms and Returns as filed by the Company with the Registrar of Companies, Regional Director, Central Government or other authorities during the financial year ending on 31st March, 20___.

1. Form No. _________________ File u/s ____________ for _________
2. Form No. _________________ File u/s ____________ for _________
3. Form No. _________________ File u/s ____________ for _________
CHECKLIST FOR COMPLIANCE CERTIFICATE

Under the ‘MCA-21’ project, the Ministry of Company Affairs has put all the Business Processes and services of the office of Registrar of Companies (ROC) on the e-Governance Mode. As such, relevant filings would need to be done mandatorily in every ROC office in the format prescribed under the new e-forms. Therefore, in view of the above, the Compliance Certificate, as provided in amended Companies (Central Government) General Rules and Forms, 1956 has to be filed along with Form No. 66 of the aforesaid rules as attachment.

1A Statutory Registers

(a) Register of Investments [Section 49(7)]

The auditor should check the following:

(a) whether all investments made by the company on its own behalf are held in its own name?

(b) whether Certificate or letter of allotment of concerned shares or securities, is in it's custody or with the banker etc. and make a physical certification of it.

(c) if the company is not holding investments made by it in its name as allowed by Sub-sections (2), (3), (4) or (5) of Section 49 verify whether:

(i) the company's principal business consists of buying and selling shares or securities or else;

(ii) the company has entered such particulars in the register maintained thereof clearly and conspicuously as may be necessary to identify fully the shares or securities in question and the bank or person in whose name or custody they are held.

(d) register is kept open for inspection of any member or debenture holder of the company, without charge, during business hours, subject to such reasonable restrictions as the company may by its articles or in general meeting impose, so that not less than two hours in each day are allowed for inspection.

(e) (i) if shares are held by directors in other body corporate check that appointment was properly made and shares in such body corporate are to an amount not exceeding qualification shares.

(ii) shares are held in its subsidiary in the nominees' name to ensure that the number of members does not fall below the statutory minimum.

(b) Register of Deposits [Rule 7 of Companies (Acceptance of Deposits) Rules, 1975]

Check:

(i) whether the company has maintained the Register of Deposits?

(ii) whether complete entries in respect of all depositors have been made?

(iii) whether the company has small depositors as per latest amendments?

(iv) Whether there has been any default in repayment of deposits or amount of interest thereon and the same is indicated clearly?

(v) compare the Register alongwith Return of Deposits filed with Registrar of
Companies.

(vi) whether the company, if an NBFC, is registered with RBI and has complied with RBI directions.

(vii) whether the register has been preserved in good order for a period of eight calendar years from the financial year in which the latest entry was made.

(c) Register of Securities Bought Back (Section 77A)

Check whether register of securities bought back has been maintained for entering the following particulars, namely, (i) the consideration paid for securities bought back; (ii) the date of cancellation of securities; (iii) the date of extinguishing and physically destroying of securities and such other particulars as prescribed in Form 4B (to be cross verified with the attachment of e-form 4C) of the Companies (Central Government’s) General Rules and Forms, 1956 and Annexure B to the Private Limited Company and Unlisted Public Limited Company (Buy-back of Securities) Rules, 1999.

(d) Register of Charges (Section 143) and Copies of Instruments Creating Charge (Section 136)

Check whether:

(i) all charges, fixed and floating on the undertaking or on any property of the company have been entered in the Register along with the details required under Section 143(1) i.e. (a) that description of the property charged, (b) amount of charge, and (c) except in case of securities of bearer the names of persons entitled in charge. Check whether date of filing of e-Form No. 8 is given in the Register.

(ii) in case of fully satisfied/repaid charges, e-Form No. 17 has been filed and entries thereof have been made in the Register.

(iv) Check if any delay is condoned by any competent authority, the date and facts of such condonation are given.

(v) the certificate of registration of charges in connection with issue of debentures is endorsed on every debenture or certificate of debenture stock issued.

(vii) whether copies of instruments creating charges in pursuance of Section 136 and register of charges pursuant to Section 143 are kept open for inspection according to Section 144.

(e) Register of Members (Section 150) and Index of Members (Section 151):

Check whether:

(i) separate registers for each class of shares are maintained in the format as prescribed under Rule 7 of the Companies (Issue of Share Certificate) Rules, 1960;

(ii) (a) the particulars relating to the name, address and the occupation, if any, of each member;

(b) in the case of a company, having a share capital, the shares held by
each member, distinguishing each share by its number except where such shares are held with a depository and the amount paid or agreed to be considered as paid on those shares;

(c) the date on which each person was entered in the register as a member;

(d) the date on which any person ceased to be a member; and

(e) Stock held, if any, by the members have been properly entered.

(iii) entries in the Register are authenticated by the Secretary or any other person authorised by the Board for the purposes of sealing and signing share certificates;

(iv) declaration made to a company under Sub-section (1), (2) or (3) of Section 187C has been noted in its Register of members within 30 days from receipt of declaration;

(v) an index of members is maintained unless the Register of members is in such a form as in itself constitutes an index, where the company has more than 50 members. The index can be in the form of a card index;

(vi) every change made in the Register of members has also been recorded in the index within 14 days; and

(vii) The index has been maintained at the same place as the register of members.

(viii) list of beneficial owners, (in case of shares held in depository) is also kept by the company.

(f) Register and Index of Debentureholders (Section 152):

Check whether:

(i) the company has maintained separate registers for each type of debentures and entered therein the particulars prescribed in Sub-section (1) of Section 152 i.e. (a) the name and address, and the occupation, if any, of each debenture holder; (b) the debentures held by each holder, distinguishing each debenture by its number except where such debentures are held with a depository, and the amount paid or agreed to be considered as paid on those debentures; (c) the date on which each person was entered in the register as a debenture holder and (d) the date at which any person ceased to be a debenture holder;

(ii) an index of debenture holders is maintained unless the Register of debenture holders is in such a form as in itself constitutes an index, where the number of debenture holders is more than 50. The index can be in the form of a card index;

(iii) every alteration made in the Register of debenture holders has been recorded in the index within 14 days;

(iv) list of beneficial owners (in case of debentures held in depository) is also kept by the company.
(g) Foreign Registers of Members or Debenture holders (Section 157):

Check whether the Articles of Association authorise for keeping a foreign register of members or debenture holders. If yes, check whether:

(i) notice of the situation of the office where registers are kept has been filed with the Registrar within 30 days from the date of the opening of any foreign register;

(ii) notice of the change, if any, in the situation of such office or of its discontinuance was filed with the Registrar within 30 days from the date of such change or discontinuance;

(iii) a duplicate of every foreign register has been kept at the registered office and changes in the register duly entered from time to time;

(iv) the above registers are kept open for inspection and extracts/copies thereof are supplied on receipt of requisition with the prescribed fees.

(h) Registers and Returns under Section 163

Check whether:

(i) the Register of members, the index of members, the Register and index of debenture holders, contracts entered into by a company for the appointment of a manager, managing director and copies of annual returns filed under Sections 159 and 160 in e-form 20B together with the copies of certificates and documents required to be annexed under Sections 160 and 161 are kept at the registered office of the company;

(ii) if the above registers and returns instead of being kept at the registered office of the company, are being kept at any other place within the city, town or village in which the registered office is situate; whether the other place has been approved by a special resolution and the Registrar was given an advance copy of the proposed special resolution;

(iii) the above registers and returns are kept open for inspection by any member or debenture holder without fee, and by any other person on payment of Rs.10/- or such other fee as may be prescribed, during business hours subject to such reasonable restrictions as the company may impose;

(iv) copy of such register etc. or extract thereof is supplied within a period of ten days against any request received on payment of Re.1 for every 100 words or fractional part thereof or such other fee as may be prescribed;

(v) the stock exchange is notified in case the shares are listed.

(i) Minutes Book of Meetings

(a) Minutes Book of Meetings of Directors

Check whether:

(i) minutes books for Board and Committee meetings are maintained in accordance with the provisions of Section 193;

(ii) the proceedings of each meeting are entered within 30 days of the meeting;
(iii) each page of the minutes book is consecutively numbered;
(iv) each page of individual minutes is duly initialled or signed and the last page of each such minutes is dated and signed by the Chairman of the same meeting or of the next succeeding meeting;
(v) names of directors present at the meeting are recorded in the minutes;
(vi) leave of absence granted is recorded;
(vii) nature of interest of a director in any transaction and also his abstaining from discussion/voting on resolution are recorded;
(viii) names of directors dissenting from or not concurring with the resolution are recorded;
(ix) minutes have not been attached or pasted to the minutes book;
(x) minutes are maintained in loose leaf form; if so whether safeguards against manipulation have been taken and the leaves are bound at reasonable intervals, say six months/one year; and
(xi) the fact that documents or drafts placed before the meeting is recorded in the minutes.

(b) Minutes Books of Proceedings of General Meetings

Check whether:

(i) minutes books are properly maintained, viz.
   — the proceedings of each general meeting have been entered within 30 days of the meeting;
   — the pages of the minutes book are consecutively numbered. Each page is duly initialled or signed and the last page of the record of proceedings of each meeting is dated and signed by the Chairman of the meeting within 30 days of the meeting;
   — in the event of death/inability of the Chairman to sign minutes of the general meeting, the Board resolution has been passed authorising any director to sign within that period;
   — the minutes are not attached or pasted. All erasures or alterations are duly authenticated;
   — the minutes are maintained in loose leaf form; if so whether safeguards against manipulation have been taken and the pages are bound at reasonable intervals, say six months/one year; and
   — the fact that documents or drafts placed before the meeting is recorded in the minutes.

(ii) minutes books have been kept at the registered office of the company and kept open during business hours for inspection of members and also, inspection is allowed to any member without charge during business hours subject to such reasonable restrictions as the company may, by Articles or in general meeting impose;
(iii) check if copies of minutes of general meetings were furnished within 7 days of the receipt of request on payment Re.1 for every 100 words or fractional part thereof or such other fee as may be prescribed.

(j) Minutes Book of Class Meeting/Creditors Meeting

Check whether company has held class meetings, debenture holders meetings or creditors meeting. If yes, whether minutes book in respect of these meetings has been properly maintained.

(k) Books of Accounts and Cost Records (Section 209)

Check whether:

(i) books of accounts are kept at the registered office. If the same are kept at some other place in India, a Board resolution was passed and e-Form No.23AA filed with the Registrar within 7 days of the decision;

(ii) the company is required to maintain cost records. If so, whether cost records are being maintained;

(iii) the books are maintained in good order together with vouchers, invoices and connected records for a minimum period of 8 years; and

(iv) books of accounts and papers were easily accessible to directors for inspection.

(v) the books of account have been maintained properly and on the accrual basis of accounting.

(vi) proper books of account relating to the transactions of a company's branch office have been kept and proper summarized returns made upto-date are sent to the place, where books of account of the company are kept at intervals not more than three months.

(l) Register of Particulars of Contracts, companies and firms in which Directors are Interested (Section 301)

Check whether:

(i) the register is being properly maintained by entering separately particulars as prescribed under Sub-section (1) of Section 301 of all contracts or arrangements to which Section 297 or Section 299 applies, ; i.e. the date of contract or management, date of placing them before the Board, the names of parties thereto, the principal terms and conditions thereof.

Where the value of goods and materials or cost of services forming part of contract or arrangement exceed one thousand rupees.

(ii) and the names of the directors voting for or against the contract or arrangement and the names of those remaining neutral are recorded

(iii) entries have been made within 7 days (including public holidays) from the date on which the Board approved the contract and in case of other contract or arrangement within seven days of the receipt at the registered office of its particulars, or within 30 days of the date of contract/arrangement whichever is later. If the company's paid-up share capital is rupees one crore or more,
check whether the previous approval of the Central Government has been obtained for entering into contracts;

(iv) the register specifies in relation to each director the names of firms and bodies corporate of which notice has been given by him under Section 299(3) [Form 24AA];

(v) the register has been signed by the directors present at the Board meeting following the meeting in which the contracts were considered and approved;

(vi) where the above contracts and/or arrangements have been approved by members in their general meeting, the register is maintained and signed in accordance with the terms of the resolution thereat; and

(vii) the register is maintained at the registered office and is kept open for inspection and extracts and copies are permitted to be taken or are given to the members in the same manner and on payment of the same fee as in the case of Register of members.

(m) Register of Directors, Managing Director, Manager and Secretary under Section 303

Check whether:

(i) the necessary particulars prescribed in Sub-section (1) of Section 303 and changes therein have been entered in respect of every director, managing director, manager or secretary;

(ii) the names and particulars of companies and/or firms nominating directors have also been entered in the register; and

(iii) the register is kept at the registered office and is kept open for inspection by members free of charge and by outsiders on payment of fee of Re.1/- during business hours subject to such reasonable restrictions as the company may by its Articles or in general meeting impose.

(iv) the disclosure is made by the concerned person within 21 days as per Section 305.

(v) requisite returns in duplicate were sent to the Registrar in Form No. 32 within 30 days of the appointment or change.

(vi) Register may be checked with Form No. 32, Annual Returns filed with Registrar and cheque signing authority to corporate bank accounts.

(vii) Where a person is a deemed director of the company, whether particulars relating to him are entered in the above Register.

(n) Register of Directors’ Shareholdings under Section 307

Check whether:

(i) the register was duly kept at the registered office and contains particulars prescribed in Sub-sections (1), (2) and (3) of Section 307 and was kept open for inspection of any member or debenture holder during business hours subject to reasonable restrictions as the company may, by its Articles or in general meeting, impose during the period beginning 14 days before the date
of the company’s annual general meeting and ending three days after the date of its conclusion, and it was kept open for inspection by any person acting on behalf of the Central Government or of the Registrar during the said period or any other period;

(ii) the register was produced at the commencement of the annual general meeting and was kept open and accessible during the continuation of the meeting to any person having the right to attend the meeting; and

(iii) every director and every person deemed to be a director under Section 307(10) has given notice in writing to the company in conformity with Section 308(1) and (2) to enable it to comply with the provisions of Section 307.

(o) Register of Investments or Loans made, Guarantee Given or Security provided under Section 372A (w.e.f. 31.10.1998)

Check whether:

(i) the register has been maintained for entering the following particulars; (a) the name of the body corporate; (b) the amount, terms and purpose of the investment or loan or security or guarantee; (c) the date on which the investment or loan has been made; and (d) the date on which the guarantee has been given or security has been provided in connection with a loan;

(ii) the particulars of every investment or loan made or guarantee given or security provided has been entered chronologically in the register within seven days of the making of such investment or loan, or the giving of such guarantee or provision of such security;

(iii) the register is kept at the registered office of the company; and the register is kept open for inspection and extracts thereof have been supplied to members, if required, on payment of the requisite fee.

Note: If the provisions of Section 372A are not applicable to a company, no entries need to be made in the Register of investments or loans made, guarantee given or security provided under Section 372A.

(p) Register of Renewed and Duplicate Certificates under Rule 7 of the Companies (Issue of Share Certificates) Rules, 1960

Check whether:

(i) the register has been maintained containing prescribed particulars, viz.; the name of the person to whom the certificate has been issued, the number and date of issue of share certificate etc.; and

(ii) all entries in the register have been authenticated by the secretary or any other person authorised by the Board of directors.

(iii) necessary entries have been made in the register of members for issuance of duplicate certificate and the original certificate, if available is cancelled.

(iv) duplicate certificates have been issued with the authority of the Board or committee and properly signed with the common seal of the company.

(v) Necessary changes have been indicated in the Register of Members by making suitable cross-references.
(q) **Register of Destruction of Records/Documents**

Check whether:

(i) the records and documents are being kept in the company at least for the periods stated in the Companies (Preservation and Disposals of Records) Rules, 1966;

(ii) the company has maintained a register in the prescribed form and has entered particulars of documents destroyed as per Rule 4 of the aforesaid Rules.

(r) **Register of Employee Stock Options**

(i) Check that if the company had issued employee stock options, it maintained a register of employee stock options and entered therein particulars of options granted.

(ii) Check whether the following details were *inter alia* and as far as applicable entered in the register viz. date of special resolution approving the scheme, category of employees entitled to participate in the scheme, total number of options granted, market price per share on the date of grant, name of the grantee, number of options granted, vesting period, options vested, exercise period, options exercised, exercise price and market price per share, number of shares arising as a result of exercise of option, options lapsed, if any variation the date of such variation, lock-in-period, date of expiry, money realised by exercise of options etc.

(iii) Check whether the register is properly maintained, preserved for a reasonable time and is open for inspection, subject to reasonable restrictions.

(s) **Register of Postal Ballot**

If the company was required to or proposed to get any resolution passed through postal ballot, check whether—

(a) a separate register was maintained for each postal ballot to record the assent or dissent received through postal ballot;

(b) particulars relating to serial number given by scrutinizer, date of receipt of postal ballot form, name, folio number/client ID number of the member, number of shares held nominal value of shares, whether the shares have voting, differential voting or non-voting rights, number of votes in favour, number of votes against, number of invalid votes and reasons therefor have been properly entered.

(c) Register along with postal ballot forms have been kept in the safe custody of the scrutinizer till the chairman signs the minutes book in which result of the voting by postal ballot is recorded.

(t) **Register of Sweat Equity Shares**

(i) Check whether a company issuing sweat equity shares has maintained a register for this purpose as required under Rule 5 of Unlisted Companies (Issue of Sweat Equity Shares) Rules, 2003 and by listed companies, in a form as near thereto.
(ii) Check whether the register contained the particulars relating to folio number/certificate number, date of passing of resolution, date of issue of sweat equity shares, name of allottee, status of the allottee, referencer to entry in register of members, number of sweat equity shares issued, face value of the share, price at which shares issued, total consideration paid by employee/director and lock-in-period.

(iii) Check whether the register is properly maintained, preserved for a reasonable period of time, and is open for inspection, subject to reasonable restrictions, if any.

(B) Other Registers

Following registers are optional registers and should be maintained as good secretarial practice. However, if the following registers are not maintained, the Practising Company Secretary should not qualify his certificate/Audit Report:

(1) Register of Inspection

Check whether the company has maintained the register of inspection containing the following particulars viz:

(i) Serial Number
(ii) Date and time of inspection
(iii) Name and address of person who has inspected the document
(iv) Particulars of documents inspected
(v) Copies, if any taken
(vi) Fees, if any received
(vii) Signature of the person who inspected the documents
(viii) Signature of a director.

Note: Maintenance of the said register would help in verifying the compliance of various provisions of the Companies Act, 1956 where records/documents are available for inspection. The register need not be kept for inspection.

(2) Register of Directors’ Attendance

As per Regulation 71 contained under Schedule-1 (Table A) to the Companies Act, 1956, every director present at any meeting of the Board or of a Committee thereof shall sign his name in a book to be kept for that purpose. In view of this, companies should maintain a register for recording the attendance of directors present in a meeting of the Board/Committee thereof.

(3) Register of Shareholders’ Attendance

Check whether the company has maintained a register of shareholders’ attendance at the general meetings or has kept the attendance slips collected from the members at the meeting.

(4) Register of Proxies

Check whether the register of proxies containing details of proxies lodged in respect of every general meeting is maintained. It may be verified whether the
particulars relating to name of member appointing proxy, folio numbers of members, number of shares held by members, name of proxy, date and time of receipt of proxy form, number of valid and invalid proxies and other relevant entries have been made chronologically.

(5) Register of Transfers/Transmission of shares

Check whether:
(i) the company has maintained separate register of transfers for different classes of shares/debentures, and entered therein the particulars relating to the registration of transfer of shares/debentures along with the date of Board/Committee resolution approving transfer/transmission;
(ii) transfer number as per the register of transfer and date of approval has been entered in the Share Transfer Deed in Form 7B;
(iii) the Company has maintained a separate file and register of documents like Powers of Attorney, Probate, Letters of Administration and/or Succession Certificate, Resolution of companies or other bodies corporate authorising any particular person(s) to sign on its behalf that are registered with the company; and
(iv) details of nomination forms have been noted.

(6) Register of Fixed Assets

Check whether the register of fixed assets has been properly maintained containing prescribed particulars of quantitative details and situation of fixed assets of the company and its updated written down values alongwith the basis of revaluation.

(7) Register of Documents Sealed

Check whether:
(i) the company has maintained a register of documents sealed;
(ii) the register contains the following information:
   (a) number and date of the resolution(s) authorising the use of the seal;
   (b) date of affixing seal;
   (c) persons in whose presence the seal was affixed;
   (d) document sealed;
   (e) location of document.

Apart from the aforesaid, registers may have been maintained in respect of Insider Trading, Substantial Acquisition of shares and Takeovers, Preferential allotment, and the same may be verified with the corresponding Rules/Regulations/Provisions in this behalf.

2. Filing of Forms, Returns and Documents with the Registrar

(A) Periodical Returns

(a) Annual Return

Check whether:
(i) e-Form-20B together with Annual return specified in Schedule V of the Act has been duly filed with the ROC within 60 days of the holding of the annual general meeting;
(ii) where annual general meeting has not been held, the return was filed within 60 days from the date on which the annual general meeting ought to have been held;
   In case of an adjourned annual general meeting, check whether the annual return incorporates the date of the original meeting.

(iii) the return has been digitally signed by the MD or Director or Manager or Secretary of the company;

(iv) in case of a company whose shares are listed on a recognised stock exchange, the annual return in Schedule V is also signed by a secretary in whole-time practice.

(v) the details in removable storage media (Floppy/compact disc) have been filed with the Registrar in case of bigger size of attachment.

(b) Balance Sheet, etc., under Section 220

Check whether:

(i) the balance sheet, etc., were adopted by the annual general meeting within the prescribed time stipulated in Section 210 read with Section 266;

(ii) copy of balance sheet along with profit and loss account and other documents so required (auditors’ report, directors’ report, corporate governance report, compliance certificate etc.) and e-form 23AC were filed with the ROC within 30 days of the date of the annual general meeting. In case of a private company, the profit and loss account may have been separately attached to e-Form 23AC;

(iii) where an annual general meeting has not been held, copies of balance sheet etc. were filed within 30 days from the latest day on or before which the meeting should have been held and whether a statement of the fact and of the reasons therefor was filed along with the balance sheet etc.;

(iv) where balance-sheet etc., were laid before but not adopted by the annual general meeting or the annual general meeting was adjourned without adopting the balance sheet, whether a statement of the fact and reasons therefor was filed along with the balance sheet, etc.

(v) whether balance sheet etc. is duly authenticated in terms of Section 215 of the Act.

(c) Compliance Certificate under Section 383A

Check whether:

(i) the company to which proviso to Sub-section (1) of Section 383A is applicable has filed with the ROC a certificate from a Practising Company Secretary in Form appended to the Companies (Compliance Certificate) Rules, 2001 along with e-Form 66 within 30 days from the date of annual general meeting.

(ii) in case the annual general meeting of the company is not held for the year, the aforesaid Compliance Certificate has been filed with the ROC within 30 days from the latest day on or before which that meeting should have been held.
(B) Other Important Returns

(a) Return of Allotment

Check whether:

(i) the company has made any allotment of its shares. If so, the return of allotment in e-Form No.2 was filed with the Registrar within 30 days stating the number and nominal amount of the shares comprised in the allotment, the names, addresses, and occupations of the allottees, and the amount, if any, paid or due and payable on each share. If the company has passed special resolution under Section 81(1A), it should also have filed e-form 23 before filing form 2 and mentioned its SRN (Service Request Number) in e-Form 2;

(ii) shares were allotted at a discount. If so, copy of the resolution authorising the issue of shares at a discount along with a copy of the order of the Company Law Board was filed with the return;

(iii) shares were issued for consideration other than cash. If so, the original contract, along with a copy thereof, entered into with the persons to whom the shares were allotted for consideration other than cash was filed with the return;

(iv) the copy of the contract was verified by an affidavit by a director or the Secretary of the company;

(v) the contract for issue of shares for consideration other than cash was not reduced in writing. If so, whether particulars of the contract were filed in e-Form No.3 and the Form was duly stamped with stamp duty which would have been paid, had the contract been reduced to writing;

(vi) bonus shares were issued. If so, a return stating the number and nominal amount of the shares comprised in the allotment, the names, address and occupation of the allottees and a copy of the resolution authorising the issue of such shares was filed;

(vii) allotment has been made in pursuance of the order of the Court under Sections 391/394. If so, verify whether shares were allotted in the proportion stated in the order.

(viii) the list of allottees is mandatorily attached to the form. Also check whether the copy of board or members’ resolution approving the shares, has been attached.

(ix) the regulator had extended the time for filing the return under Section 75(3) and the return was duly filed in the extended time period;

Notes:
1. The return of allotment is not required to be filed in case the allotment was of forfeited shares or the allotment was made to the subscriber to the Memorandum and Articles of Association.

2. The return of allotment is not required to be filed where debentures are allotted.
(b) Return on Buy-Back of Securities

(i) Check whether the company has filed with the Registrar, e-Form No. 4C under the Companies (Central Government’s) General Rules and Forms, 1956 (as amended) and a return in the form specified at Annexure A to the Private Limited Company and Unlisted Public Limited Company (Buy-Back of Securities) Rules, 1999 after the completion of buy-back.

(ii) Check whether the return (e-form 4C) is filed with the Registrar within 30 days from the completion of the buy-back.

(iii) Check that where the company was required to file e-form 23 in relation to the resolution passed for buy-back, filing of e-form 23 preceded the filing of this return and SRN of Form 23 has been entered in e-form 4C.

(iv) Check whether any Merchant Banker was appointed, and if so, whether his name has been entered in the form.

(v) Check that the following documents were attached to the e-form 4C viz. description of securities bought back by the company (in the prescribed format); particulars relating to the holder of securities before buy-back (in the prescribed format); copy of special resolution, if any; copy of Board resolution in case buy-back was approved by the Board etc.

(vi) Check whether e-form 62 is submitted together with the filing fees.

(c) Notice of redemption of preference shares, consolidation, division, increase in share capital, cancellation of shares and increase in number of members

Check whether:

(i) the requisite notice in e-Form No.5 was filed within 30 days from the day on which any of the aforesaid events occurred or resolution passed as the case may be; and

(ii) e-Form 23 had been filed where special resolution was passed for such alterations and SRN of e-Form 23 is mentioned in the form;

(iii) in case there is consolidation/sub-division/cancellation for both equity and preference shares, then a separate e-form is filed for each category of shares;

(iv) in case, the authorized share capital is increased both independently and by Central Government Order then the details of the total additional authorized capital for equity and preference shares had been duly entered in the e-form 5.

(v) the attachments viz altered memorandum of association, articles of association, proof of Central Government order for increase in authorised share capital, had been duly sent along with the form;

(vi) the e-form had been duly certified by a chartered accountant, or cost accountant or company secretary (in whole-time practice) by digitally signing the e-form;

(vii) requisite registration fees have been paid on the difference between the increased capital and the existing authorised capital at the existing rate.
(d) Notice of Situation/Change in Situation of Registered Office

Check whether:

(i) the notice of situation or the notice of change in the situation of registered office in e-Form-18 has been filed within 30 days of the date of incorporation or change;

(ii) Form 18 is pre-certified by a company secretary or chartered accountant or cost accountant in whole-time practice;

(iii) A copy of the Board resolution had been attached in case the company's registered office was shifted within the local limits of the city or town or village in which it was earlier situated;

(iv) A copy of special resolution was attached, in case the company's registered office was shifted outside the local limits of the city or town or village in which it was earlier situated and form 23 was duly filed.

(v) in addition to the above, check also the following (if applicable):

(a) in the case of change in the situation of the registered office outside the local limits of any city, town or village though within the same State but from the jurisdiction of one ROC to the jurisdiction of another ROC, check whether:

   (i) application in e-Form 1AD for obtaining confirmation of Regional Director;

   (ii) confirmation from Regional Director has been received;

   (iii) certified copy of the confirmation has been filed with the ROC within two months from the date of confirmation;

   (iv) Form No. 23 has been filed within 30 days along with the copy of special resolution passed by the company (to be passed by postal ballot in case of listed companies);

   (v) Form No. 18 has been filed with both the ROCs within 30 days of changing the office with both the Registrars;

   (vi) the ROC has certified the registration.

   (vii) Form No. 21 has been filed along with the certified copy of the order of the Company Law Board with both the ROCs within three months.

(c) in the case of change in situation of the registered office from one State to another, check whether:

   (i) e-Form 23 has been filed with ROCs within 30 days of passing of resolution;

   (ii) petition has been made to Company Law Board for approval;

   (iii) As stated aforesaid Form No. 18 has been filed with both the ROCs within 30 days from the date when the change becomes effective and Form 21 has been filed with both the ROCs within three
months.

(e) Court/CLB Orders

Check whether e-Form No.21 has been filed with the ROC along with certified copies of the following orders:

**Section**

17(2) Order of the Company Law Board approving the shifting of the registered office from one State to other.

79 Order of the Company Law Board approving Issue of shares at discount.

81(4) Order of the Central Government for conversion of debentures or loans or part thereof into shares of the company, subject to specified conditions, if found necessary in the public interest.

81(3) Order of the Central Government approving the terms of issue of debentures relating to conversion of debenture or loan into shares.

94A(2) Order of the Central Government permitting public financial institution to convert debentures or loan into shares.

102(1) Order of the Court confirming the reduction of capital.

107(3) Order of the Court disallowing or confirming variation of the shareholders rights.

111(5) or 111A Order of the Company Law Board dismissing the appeal or rejecting the application in respect of refusal of registration of transfer and directing that the transfer or transmission shall be registered by the company/directing the rectification of the register of members.

113 Order of the Company Law Board granting extension of time for issue of debenture certificate.

141 Order of the Company Law Board extending time for filing particulars of registration, modification or satisfaction of charges or rectifying the register of charges.

186 Order of the Company Law Board for a meeting of the company to be called, held and conducted in terms of the Order.

391(2) Order of the Court sanctioning any compromise or arrangement.

394(2) Order of the Court making provisions for several matters specified in Section 394(1) for implementing the compromise or arrangement.

397 Order of CLB for relief in cases of oppression

398 Order of CLB for relief in cases of mismanagement

404(3) Order of the Company Law Board providing for change in Memorandum or Articles.

445 Order of CLB for winding up passed under section 443 to be filed with Registrar.

481 Order of CLB for the dissolution of the company.

It should be ensured that the original certified copies of the Court or CLB Orders
were also submitted simultaneously at the concerned ROC office.

(f) Registration of Resolutions and Agreements

Check whether copies of resolutions and agreements required to be filed along with e-Form No. 23 with the ROC under Section 192 have been filed within 30 days after the passing of the resolution or the making of the agreement.

(g) Return of Appointment of Managing Director/Whole-time Director/Manager

Check whether:

(i) a return in e-Form No. 25C is filed within 90 days from the date of appointment of Managing Director or Whole-time Director/Manager;

(ii) the certification with respect to compliance of all the requirements of Schedule XIII has been given by the auditor or secretary of the company. Also, it has been pre-certified by a Chartered Accountant or Cost accountant or a Secretary in whole-time practice.

(iii) the Director Identification Number (DIN) has been duly entered in case of a director and the PAN had been entered in the case of a manager in the Form.

(iv) Copy of the board resolution and copy of the shareholder(s) resolution, if any had been duly attached to the form.

(v) The particulars in e-form 23, in respect of appointment of managing director or reappointment or variation of the terms have been filed with the Registrar within 30 days of the appointment. (This provision is not applicable to appointment of whole-time director and manager.

(vi) Whether Form 32 was also filed with the Registrar in case an existing director was appointed managing director or manager or where the appointment was so made for the first time.

(h) Consent to Act as Director of the Company (in the Case of Public Company)

Check whether the director other than those specified in Sub-section (2) of Section 264 has filed with the Registrar his consent to act as director on a plain paper attached to e-Form No. 32 within 30 days of his appointment.

Note: If an undertaking for acquiring qualification shares is made, the undertaking should be given on a stamp paper of requisite value and the same should be attached to e-Form 32.

(i) Particulars of Appointment of Directors, Managing Director, Manager, or Secretary and Changes thereof [Section 303(2)]

Check whether:

(i) the requisite returns had been filed with the ROC in e-Form No. 32 within 30 days of appointment/change in director, managing director, manager or secretary along with documents evidencing the same;

(ii) upon the change in particulars of director to a managing/whole-time director or an additional director being appointed as a director at annual general
meeting, the fact has been notified in e-Form No. 32 also.

(iii) The Director Identification Number (DIN) had been duly entered in case of director and the Permanent Account Number (PAN) in case of manager or secretary, had been mentioned.

(iv) The particulars of changes for more than three persons had been notified to the Registrar by using the Addendum to e-form 32.

(v) The photograph of the persons appointed was duly attached to e-form 32 and in case of consent required, the consent letter of the appointee was attached.

(vi) If an undertaking to take qualification shares was given, the evidence of payment of stamp duty was also attached to the form. Also, the original attachment relating to qualification shares was duly filled in and signed on stamp paper and was sent to the concerned ROC office simultaneously.

(j) Return of Deposits under Section 58A

Check whether:

(i) the company has on or before 30th day of June, filed with the Registrar a return in the form annexed to Companies (Acceptance of Deposits) Rules, 1975 duly certified by the auditor of the company along with e-Form 62;

(ii) a copy of the return has simultaneously been furnished to Reserve Bank of India.

(k) Particulars of Beneficial Interest in Shares

Check whether-

(i) E-form 22B has been filed with ROC within 30 days of receipt of declaration under section 187C.

(ii) The declarations under section 187(4), (2) and/or (3) had been attached to the form.*

(l) Registration of Creation/Modification/Satisfaction of Charge

Check whether:

(i) the charge falls within any one of the categories of registrable charges as provided in Sub-section (4) of Section 125;

(ii) the prescribed particulars of the charge requiring registration were filed with the ROC in e-Form No. 8 digitally signed by the company as well as the charge-holder and along with the original/certified copy of the instrument, if any, within 30 days after the date of its creation or within the time permitted by the ROC under proviso to Sub-section (1) of Section 125 of the Companies Act;

(iii) The e-Form 8 was pre-certified by a Practising Company Secretary or Chartered accountant or Cost accountant;

(iv) in case of issue of debentures of a series, if there has been any charge to the

* Form 22B is a new form which seeks to replace Form III under Companies (Declaration of Beneficial Interest in Shares) Rules, 1975.
benefit of debenture holders of that series, the required particulars have been filed with the Registrar in Form No. 10 (Form 10 should also have been pre-certified as above) within 30 days from the date of execution of the debentures of the series;

(v) in case commission, allowance, discount is paid or made in consideration for subscribing, etc., to debentures, whether the forms included particulars of such commission, etc.;

(vi) the documents were duly registered by the ROC or a Charge Identification Number was allotted;

(vii) abstract of registration is duly endorsed on every debenture or certificate of debenture stock issued, the payment of which is secured by the charge registered;

(viii) particulars of modification of charges were filed in e-Form No.8 duly signed with the ROC within 30 days of the modification or within the extended period;

(ix) a copy of the instrument creating/modifying charge/a copy of debenture of the series, if any, required to be registered was kept at the registered office;

(x) where payment or satisfaction of charge registered has been effected in full, intimation thereof has been sent to the ROC in e-Form No.17 by the company as well as the charge- holder within 30 days from the date of such payment or satisfaction (Section 138);

(xi) the satisfaction of charge has been registered by the ROC.

(xii) in case of delay/omission/mis-statement in filing particulars of charge created/modified or issue of debentures of a series or intimation of satisfaction of charge, to the ROC a petition has been made to the Company Law Board in accordance with the Company Law Board Regulations, 1991 and CLB order obtained and certified copy of such order has been furnished to the ROC along with e-Form No. 21.

(C) Forms, Returns and Documents to be Filed with other Authorities

Check whether forms, returns and documents have been filed with the other authorities wherever applicable, as mentioned below:

(1) intimation has been given to the Company Law Board in respect of any default made by the company in repayment of any deposits from small depositors within 60 days from the date of default. Intimation shall be given on monthly basis;

(2) copy of Return of Deposits of a non-banking non financial company has been filed with the Reserve Bank of India pursuant to Rule 10 of the Companies (Acceptance of Deposits) Rules, 1975;

(3) text of advertisement inviting deposits by a non-banking financial company has been filed with the Reserve Bank of India pursuant to Rule 5 of the Non-Banking Financial Companies And Misc. Non-Banking Companies (Advertisement) Rules, 1977;

(4) returns have been filed with the Securities and Exchange Board of India in
case of buy-back of securities;

(5) intimations required to be given to the Official Liquidator/Courts when the company is in the process of winding up/amalgamation/merger/reconstruction have been given;

(6) report by public companies in relation to Disqualification of Directors pursuant to Section 274 1(g) and Rules thereunder have been given;

(7) statement of amount(s) credited to Investor Education and Protection Fund have been duly furnished;

3. Status of the Company

(a) In case of Private Company

Check whether:

(i) the company has a minimum paid up capital of Rs.1 lakh or such higher paid-up capital as may be prescribed from time to time. In case of an existing private company this requirement was to be complied within a period of two years from the commencement of the Companies (Amendment) Act, 2000 i.e. from 13.12.2000;

(ii) company's articles contain provisions

(a) restricting the right to transfer its shares;

(b) limiting the number of members to fifty;

(c) prohibiting any invitation to public to subscribe to its shares/debentures; and

(d) prohibiting any invitation or acceptance of deposits from persons other than its members, directors or their relatives.

(iii) Whether the existing number of members with reference to the Register of Members is fifty. If it exceeds fifty, ascertain the number of present employees who are members of the company and number of persons, who were previously employees as well as members and who have continued to be members, after their employment ceased, and find, whether after deducting the number of present and past employees, the total number of members exceeds fifty.

(b) In case of Private Company which is a Subsidiary of a Public Company

Check whether the company has a minimum paid-up capital of 5 lakh rupees or such higher paid up capital, as may be prescribed from time to time. In case of existing public limited company, check that it has enhanced its paid up capital to five lakh rupees within two years from the commencement of the Companies (Amendment) Act, 2000 i.e. 13.12.2000.

Note: A company registered under Section 25 before or after the commencement of the Companies (Amendment) Act, 2000 shall not be required to have minimum paid up capital specified above. However, a guarantee company having share capital
should have minimum paid-up capital specified above.

4. Meetings of Directors and Minutes

Check whether:

(i) the requisite number of Board meetings as required under Section 285 of the Companies Act and in case of listed companies, also as required under Clause 49 of Listing Agreement were held during the year;

(ii) notice of each Board meeting in writing was issued to every director for the time being in India and at his usual address in India to every other director;

(iii) attendance-records are maintained and the requirements of Board meetings regarding quorum, chairman, minutes etc., have been complied with;

(iv) whether a meeting had been adjourned for want of quorum and at the adjourned meeting quorum was present.

(v) the items required to be transacted only at the meeting of the Board were actually transacted at the meeting and not by way of resolution by circulation or otherwise;*

(vi) every director has disclosed his interest at the Board meeting where transaction is considered in which he is directly or indirectly interested and the interested director has abstained from participating or voting at such meeting and the notices of disclosure of general interest under Section 299 have been received from all the directors before the close of the financial year and placed before and read at the next Board meeting and entries thereof have been made in the Register under Section 301 and noted by the Board and renewed every year;

Note: Interested directors of a private company need not abstain from participating or voting.

(vii) Whether any item of business which has been not included in the agenda

* In the following cases, the resolution can be passed by the Board by circulation:
  (a) Filing up of casual vacancy in the office of a director appointed in a General Meeting [Section 262(1)].
  (b) To make calls on members [Section 292(1)(a)].
  (c) To authorize, the buy-back referred to in the first proviso to clause (b) of sub-section (2) of section 77A [section 292(1)(aa)].
  (d) To issue debentures [Section 292(1)(b)].
  (e) To borrow money otherwise than above [Section 292(1)(c)].
  (f) To invest funds [Section 292(1)(d)].
  (g) To make loans [section 292(1)(e)].
  (h) To delegate powers [Section 292(1)(c)(d) and (e)].
  (i) To approve contracts in which directors are interested [Section 297].
  (j) To note the general disclosure of directors’ interests or the general notice or renewal thereof [Section 299].
  (k) To note disclosure of shareholdings of directors and manager [Section 307].
  (l) In case of a public company,
      (i) to appoint a person as manager or managing director in more than one company [Section 316 and 386].
      (ii) Make inter corporate loans and investment [Section 372A].
taken up at the meeting, with the permission of the Board.

(viii) the Board had constituted any committees; if so whether requirements regarding quorum, chairman, minutes, etc., of committee meetings were duly complied with;

(ix) the minutes of committee meetings were regularly placed before the Board for taking note of;

(x) the draft of the resolutions proposed to be passed by circulation together with necessary papers were circulated to all the directors then in India and their number was not less than the quorum fixed for the Board meeting and to all the other directors at their usual addresses in India;

(xi) the resolution by circulation was approved by requisite number of directors as required under Section 289;

(xii) the resolutions passed by circulation were put up at the next Board meeting for taking note of.

(xiii) the company being a Producer company, then provisions of section 58V of the Act have been complied with.

5. Closure of Register of Members or Debentureholders

Check whether:

(i) the Register of members or debentureholders was closed during the year;

(ii) the period for which it was closed did not exceed, in the aggregate, forty five days in a year and not for more than thirty days at any one time.

(iii) not less than seven days’ previous notice was given by advertisement in some newspaper circulating in the district in which the registered office of the company is situated, to close the register;

(iv) the company has kept foreign register of members or debentureholders; if so, whether an advertisement has been given in some newspaper circulating in the district wherein the foreign register is kept where the company closes its register of members/debentureholders.

Note: Normally this register is closed only before the annual general meeting and for other purposes record dates may be fixed only by listed companies. This requirement will not normally apply to a private company.

6.(a) Annual General Meeting and Minutes

Check whether:

(i) the first annual general meeting was held within 18 months from the date of incorporation of the company.

(ii) subsequent annual general meetings have been held in each year (calendar year) and the gap between two successive annual general meetings has not been more than 15 months or the period extended by the ROC as the case may be;

(iii) the Board of Directors had approved the notice of annual general meeting
including the business to be transacted thereat, the time, date and place of the meeting;

(iv) a private company has by its articles and a resolution agreed to by all the members, fixed the time as well as place of annual general meeting;

(v) the provisions of Section 210 read with Section 166 have been complied with and if not whether an application for extension was made to ROC concerned;

(vi) meetings have been called during business hours on a day not being a public holiday and held at the registered office of the company or at any place in the same city, town or village;

(vii) provisions of Sections 171 to 193 and other requirements e.g., notice, quorum, chairman, proxy, attendance, placing and reading of Auditors’ report, placing instruments of proxy, proxy register and register of directors' shareholdings, conduct of meeting and preparation and signing of minutes etc., were complied with (if the meetings were called at a shorter notice, the same should have been consented to by all members in writing in Form 22A).

Note: Provisions of Sections 171 to 186 do not apply to private companies if the Articles of Association so provide.

(b) Sending of Notices, etc. to the Members

Check whether:

(i) a copy of the balance sheet, auditors’ report, Boards’ report along with a copy of the compliance certificate and other specified documents including notice of the meeting were sent to members, trustees of debentureholders, auditors, etc. free of cost at least 21 clear days before the meeting. If sent less than 21 clear days before the meeting whether such shorter period was agreed to by all the members. If any directions were received from the Central Government for circulation of the cost audit report to the members along with the notice of the annual general meeting, whether the same has been complied with;

(ii) in case the shares of the company are listed on a stock exchange ensure that the company has supplied a copy of the complete and full balance sheet and profit and loss account and the directors report to shareholders as provided under Clause 32 of the listing agreement though abridged accounts could be sent pursuant to Section 219(1)(b)(iv) in Form 23AB;

(iii) a copy of the unabridged annual report was sent to members, debenture-holders and depositors on demand, without charge, within 7 days of the requisition.

Minutes Books of Proceeding of General Meetings

Check

(i) Whether Minutes books are properly maintained;

— the proceedings of each meeting have been entered within 30 days of the meeting:

— the pages of the minutes book are consecutively numbered. Each page is duly initialed or signed and the last page of the record of proceedings
of each meeting is dated and signed by the Chairman of the meeting within 30 days of the meeting;

— in the event of death/inability of the Chairman to sign minutes of the general meeting, the Board resolution has been passed authorizing any director to sign within that period;

— the minutes are not attached or pasted. All erasures or alterations are duly authenticated;

— the minutes are maintained in loose leaf form; if so whether safeguards against manipulation have been taken and the pages are bound at reasonable intervals, say six months/one year; and

— the fact that documents or drafts placed before the meeting is recorded in the minutes.

(ii) minutes books have been kept at the registered office of the company and kept open during business hours for inspection of members and also, inspection is allowed to any member without charge during business hours subject to such reasonable restrictions as the company may, by Articles or in general meeting impose.

(iii) check if copies of minutes of general meetings were furnished within 7 days of the receipt of request on payment Re.1 for every 100 words or fractional part thereof or such other fee as may be prescribed.

7. Extraordinary General Meeting

Check whether:

(i) requirements relating to notice, attendance, Chairman, quorum, proxy, proxy register/instruments of proxy and proper conduct of meeting as well as maintenance of minutes of a general meeting have been complied with (whether 95% of the members had agreed in writing, before the meeting was convened on a shorter notice);

(ii) in case of meetings on requisition,

(a) the requisition has set out the matters for consideration and has been signed by members holding not less than 1/10th of the paid-up capital with voting rights or 1/10th of the total voting power, as the case may be;

(b) the requisition had been deposited at the registered office of the company;

(c) the Board, within 21 days of deposit of a valid requisition has proceeded to call a meeting on a day within 45 days from the date of deposit of such requisition;

(d) in case the meeting has been called by requisitionists, reasonable expenses incurred by them have been reimbursed by the company and this sum has been recovered from the defaulting directors.

(e) whether the proceedings of the meeting have been duly minuted.

8. Loans to Directors

Check whether provisions of Section 295(2) are applicable. If applicable check
whether:

(a) check whether provisions of Section 292(1)(c) and 372A are applicable and if so, have been complied with. If applicable, check whether, any loan has been made to:

(i) any director of the lending company
(ii) any director of the holding company
(iii) any partner of any such director
(iv) any relative of any such director
(v) any firm in which any such director is a partner
(vi) any firm in which a relative of such a director is a partner
(vii) any private company of which any such director is a director.
(viii) any private company of which any such director is a member
(ix) any body corporate of which not less than 25% of the total voting power may be exercised or controlled at a general meeting by any director or by two or more directors together; and
(x) any body corporate, the Board of directors, managing director or manager whereof is accustomed to act in accordance with the directions or instructions of the Board, or any director or directors, of the lending company.

(b) the previous approval of the Central Government as per Section 295 (except housing loan to a managing director as per the guidelines issued by the Central Government) has been obtained. (i.e. in form 24AB)

(c) The application has to be submitted with following enclosures in the PDF files:

(1) Copy of the Board resolution indicating the proposal of the company, terms and conditions, interest of directors or relatives, if any, specifying rate of interest chargeable, the schedule and terms of repayment, the loan is not being made out of borrowed funds of the company.

(2) Any other major or important condition having bearing on the loan or financial position of the company.

(3) A declaration that company has not defaulted in making repayments to the investors as and when they become due to them.

(4) Copy of draft loan agreement.

(5) Declaration to the effect that funds proposed to be loaned are not required for its working capital requirements at least for a year.

(6) A declaration from the statutory auditor or a company secretary in whole-time practice that:-

(i) The company has not defaulted in:
   — The repayment of any fixed deposits or part thereof or interest thereon;
   — Payment of dividend;
   — Redemption or repayment of debenture and timely payment
of interest thereon;
   — Redemption of preference shares; and
(ii) The company is regular in filing all e-forms or returns as required to be filed under the Companies Act, 1956;
(iii) The proposal is in conformity with the provisions of section 372A of the Companies Act, 1956;
(iv) The company is not in any default on account of undisputed dues of the Central Government e.g., income tax, central excise etc. For this purpose, the status of disputed and undisputed dues shall be made available so as to enable the Ministry to form a view in the matter vis-à-vis the coverage thereof available and assessed against the Net Worth/Profits of the applicant company.

(7) Copy of member resolution containing specific approval of required members along with explanatory statement.

(8) List of directors of board of both the companies and disclosing inter-se interest if any.

(9) Copy of loan scheme for the employees of the company, if any.

(10) No objection certificate (NOC) or prior approval of public financial institutions or banks in case any term loan is subsisting.

(11) Copy of letter from bank or financial institutions wherein the company has been asked to furnish corporate guarantee or security for the loan sanctioned to the borrower company.

(12) Shareholding pattern of applicant and borrowing company.

(13) Certified copy of the Memorandum and Articles.

(14) Certified copy of the balance sheet and profit and loss account of the company for last three years.

(d) check whether Form 24AB was pre-certified by a chartered accountant, cost accountant or company secretary in whole-time practice.

(e) Any quantity of such loan, guarantee or security is outstanding at the end of financial year.

(f) whether necessary entries have been made in register of loans.

(g) Also, whether the case was exempted by virtue of the following clarifications issued by Central Government in respect of Section 297:

Section 297 (1) does not apply to
(a) the employment as managing director/whole-time director
(b) appointment of additional directors
(c) transactions in respect of immovable property
(d) services of a legal practitioner
(e) contract of personal services
(f) contracts on principal to principal basis
(g) sale or purchase for cash

**Note:** Relevant ledger accounts should also be verified.

**9. Board's Sanction for Certain Contracts**

Check if exemptions provided in Sub-section (2) of Section 297 were applicable. If not, check whether:

(i) Board of directors’ consent was obtained by a resolution passed at a meeting for entering into contracts in which directors were interested;

(ii) Board approved the contract by passing a resolution at a Board meeting, before the contract is entered into or within three months of the date on which it was entered into;

(iii) Where the Contracts were entered in cases of emergency, whether these complied with the provisions regarding resolution to be passed in the context;

(iv) Proper quorum was present and an interested director did not participate or vote at that meeting;

(v) Regional Director’s prior approval was obtained if the paid-up share capital of the company was not less than rupees one crore by filing e-form 24A;

(vi) whether e-form 24A was accompanied by the attachments relating to copy of agreement containing particulars of contract, copy of board resolution and proceedings of meeting, a detailed application pertaining to the Act that whether the terms of the contract conform to the prevailing market rates and whether the company has entered into any contract with any other person in respect of sale, purchase or supply etc. and whether the terms of such contract are similar to the terms of the proposed contract(s).

(vii) the particulars of contract were entered in the register of contracts in accordance with Section 301.

**Note:** Relevant ledger accounts should also be verified.

**Entries in Register of Contracts**

Check whether:

(i) the register is being properly maintained by separately entering particulars as prescribed under sub-section (1) of section 301, of all contracts or arrangements to which section 297 or section 299 applies;

(ii) the names of the directors voting for or against the contract or arrangement and the names of those remaining neutral are recorded;

(iii) entries have been made within 7 days from the date on which contract or arrangement was made. If the company's paid-up share capital is rupees one crore or more, check whether the previous approval of the Central Government has been obtained for entering into contracts;

(iv) the register specifies in relation to each director the names of firms and bodies corporate of which notice has been given by him under section
the register has been signed by the directors present at the Board meeting following the meeting in which the contracts were considered;

(vi) where the above contracts and/or arrangements have been approved by members in their general meeting, the register is maintained and signed in accordance with the terms of the resolution thereat; and

(vii) the register is maintained at the registered office and is kept open for inspection and extracts and copies are permitted to be taken or are given to the members in the same manner and on payment of the same fee as in the case of Register of members.

10. Holding Office or Place of Profit

Check whether:

(i) a director of the company and others referred to in Clause (b) of Sub-section (1) of Section 314 hold any office or place of profit;

(ii) necessary declaration was obtained from persons referred to in Sub-section (2A) of Section 314;

(iii) a prior special resolution was duly passed at the general meeting and e-Form No. 23 was duly filed with the Registrar;

(iv) whether the total monthly remuneration was Rs. 10,000 or more;

(v) approval of the Central Government was obtained where monthly remuneration paid was not less than Rs. 50,000/-, or as may be prescribed from time to time in e-form 24B;

(vi) Form 24B was accompanied by:

(a) copy of the resolution passed by the board of directors, relating to the proposed appointment.

(b) copy of rules of company relating to terms and conditions in regard to perquisites as applicable to its employees

(c) shareholding pattern of the company etc.

(vii) the person concerned was rendering professional advice (in which case section 314(1) is not applicable).

(viii) the concerned person vacated his office immediately and refunded the remuneration received from the company if the Central Government's permission was either not obtained or denied.

Note: Relevant ledger accounts should also be verified.

11. Issue of Duplicate Share Certificates

Check whether:

(i) duplicate certificates have been issued with the prior consent of the Board or Committee thereof as also in accordance with the provisions of Section 84 of the Act;
(ii) both strength and quorum of the Committee of directors constituted under Rule 3(b) of the Companies (Issue of Share Certificates) Rules, 1960, are not less than 3 directors where the total number of directors of the company exceeds 6 and not less than 2 directors where the total number does not exceed 6 and to the extent the composition of the Board of directors permits, half of the number of members of the Committee are directors other than a managing director or whole-time director;

(iii) the Board resolution for issue of duplicate share certificates has been passed;

(iv) the form of certificate including split/consolidated/replaced/duplicate issued conforms to Rule 5 of the said Rules;

(v) certificates issued by the company comply with Rule 6 of the said Rules as to affixing seal and signing of certificates;

(vi) (a) particulars of every share certificate issued in the Register of members have been recorded;
     (b) particulars of every share certificate issued for split/consolidation or duplicate certificate issued are recorded in the register of renewed/consolidated and duplicate certificate issued;
     (c) all entries made in the Register of members or register of renewed or duplicate certificates have been authenticated by the Secretary or such other persons as may be appointed by the Board.

(vii) the company has a good internal control system for blank form of share certificate and all certificates issued and blank stationery have been periodically accounted to the Board;

(viii) all books and documents relating to the issue of share certificates have been preserved in good order permanently;

(ix) appropriate indemnity bond and affidavit have been obtained.

(x) an advertisement was released in case articles so require.

12. Issue of Certificates, Transfer/Transmission of Shares, Dividend, Board's Report

(a) Issue of Certificates for Shares and other Securities

Check whether:

(i) the company has allotted shares/debentures and entered the names of allottees in its register of members/debentureholders;

(ii) the company has issued and delivered share-certificates as per Sections 83 and 113 of the Act and the provisions of the Companies (Issue of Share Certificates) Rules, 1960;

(iii) the company has executed Debenture Trust Deed in case of secured debentures;

(iv) the company has delivered debenture-certificates within the prescribed period and in case of delay, CLB Order for extension of time has been obtained;
(v) the company has registered transfer and transmission of shares as per Sections 108 to 113;
(vi) the company has kept in abeyance the registration of transfers in cases of Court-injunction.

(b) Transfer and Transmission of Shares

I. Transfer of Shares

Check whether:

(i) the requirements contained in the Articles of Association have been complied with;
(ii) the transfer of shares/debentures and the issue of certificates thereof have been made within the stipulated time under Sections 108 and 113 in accordance with the procedures prescribed;
(iii) in respect of transfer deeds reported lost, the company has registered transfer of shares based on an application in writing on stamp paper of the required value with indemnity duly executed by the transferee to the satisfaction of the Board in accordance with the first proviso to Section 108(1);
(iv) transfer applications duly executed by the transferor and transferee completed in all respects are delivered to the company within the validity period mentioned in Section 108(1A);
(v) share transfer application is in Form 7B/7BB, as the case may be;
(vi) a notice had been sent to the transferee in case of application for transfer of partly paid shares pursuant to section 110(2) and (3);
(vii) requisite permission under Section 108A, 108B and 108C has been obtained from the Central Government in applicable cases;
(viii) any directions issued by the Central Government under Section 108D has been complied with;
(ix) Central Government or CLB/Tribunal has not imposed any restriction on transfer [Section 247, 248, 250 etc.]
(x) nomination of shares/debentures received under Section 109A has been duly noted on relevant registers by the company;
(xi) the shares/debentures have not been registered in the name of a firm, HUF, trust (unless registered under Societies Registration Act, 1860), in view of the provisions under Section 153;
(xii) certification of transfer was done in accordance with the provisions under Section 112. If yes, check whether the certification on the instrument of transfer to the effect "certificate lodged" was done by a duly authorised person; and
(xiii) all transfers have been properly included in the Annual Return.

Note: Practising Company Secretary should also verify entries in the register of
transfers.

The provisions of section 108 will not apply to transfer of security by the transferor and transferee, both of whom are entered as beneficial owners in the records of a depository.

II. Transmission of shares

Check whether:

(a) a person had been nominated to whom the shares/debentures were to vest in the event of death in Form 2B;

(b) the shares have been transmitted to the legal representative of the deceased shareholder in the case of death of a sole shareholder and in the case of joint holdings only to the survivor(s);

(c) transmission of shares is effected upon the production of succession certificate or probate or letter of administration or indemnity duly signed by the legal heirs of the deceased or as per procedure stipulated by the Board of directors and/or Articles of Association.

(c) Declaration, Payment and Transfer of Dividend

Check whether:

(i) dividends were declared out of profits after providing for depreciation according to the provisions of Section 205(2) (unless an exemption in this regard was obtained);

(ii) specified minimum amount has been transferred to reserves according to the Companies (Transfer of Profits to Reserves) Rules, 1975;

(iii) Board resolution recommending dividend has been passed;

(iv) the Board has authorised the opening of a separate Bank Account for payment of dividend;

(v) the amount of dividend including interim dividend was deposited in the separate Bank Account within 5 days from the date of declaration of such dividend;

(vi) register of members was closed as per the provisions of Section 154;

(vii) interim dividend, if any, declared by the Board of directors has been confirmed/noted at the annual general meeting;

(viii) dividend recommended by the Board was declared at the annual general meeting;

(ix) dividend warrants were printed, signed and despatched to the registered shareholders within 30 days of declaration;

(x) permission of Reserve Bank of India, if required was obtained before dividend was remitted to foreigners/non resident Indians;

(xi) stock exchanges were duly intimated, in case of listed company;

(xii) voluntary transfer to reserves, if any, was made according to the Companies (Transfer of Profits to Reserves) Rules, 1975;
(xiii) in case of inadequacy of profits, the Companies (Declaration of Dividends out of Reserves) Rules, 1975, were complied with or previous approval of the Central Government was obtained, before such declaration by (e-filing) of form pursuant to such rules, duly precertified;

(xiv) dividends were paid in accordance with Section 206 only to the registered shareholder or his order or to his bankers. In case of a share warrant, dividend has been paid to the bearer of such warrant or to his bankers;

(xv) unpaid or unclaimed dividend was transferred to the unpaid dividend account within 7 days after the expiry of 30 days from the date of declaration (Section 205A);

(xvi) amount of dividend remaining unpaid and unclaimed for seven years from the date they became due for payment has been transferred to the Investor Education and Protection Fund, established by the Central Government pursuant to Section 205C and while transferring the amount, the company furnished a statement in the prescribed form under Section 205A(6).

(xvii) where duplicate dividend warrants were issued, whether indemnity in lieu of dividend warrants lost/defaced were obtained.

(d) Board’s Report

Check whether:

(i) a Board resolution was passed authorising chairman or other directors to sign the report on behalf of the Board;

(ii) the report and any addendum thereto was duly signed by persons authorised to sign;

(iii) the Board’s report was attached to the balance sheet;

(iv) the report contained specified particulars viz. state of affairs of the company, proposed transfer to reserves, proposed dividend, material changes affecting the financial position, conservation of energy, technology absorption, etc. Also whether the requirements specified in Companies (Disclosure of Particulars in the Report of Board of Directors Rules), 1988 have been complied with;

(v) the Board’s report includes a statement showing employees particulars in accordance with the Companies (Particulars of Employees) Rules, 1975;

(vi) the Board’s report includes a Directors Responsibility Statement, about:

— following applicable accounting standards
— consistent application of accounting policies
— maintenance of adequate accounting records
— preparation of annual accounts on going concern basis;

(vii) in the case of a Non-Banking Financial Company, a Residuary Non-banking company, the Board’s report includes details required to be furnished under Non-Banking Financial Companies (Reserve Bank) Directions, 1988/Residuary Non-Banking Companies (Reserve Bank) Directions, 1987, as the case may be;
(viii) in case the company has passed a special resolution to purchase its own securities (Buy-back) pursuant to Section 77A and the Buy-back has not been completed within the time specified (12 months from the date of the resolution), the reasons for failure have been specified;

(ix) a copy of the Compliance Certificate issued by a Practising Company Secretary was attached to the Board’s report;

(x) the Board’s report gives the fullest information and explanations on every reservation, qualifications or adverse remarks, if any contained in the auditors report;

(xi) changes in the directors of the company have been reported.

(e) Transfer of Unpaid Amounts to the Investor Education and Protection Fund

(i) Check whether the company has duly transferred the following amounts to the Investor Education and Protection Fund:

(a) amounts in the unpaid dividend accounts of the company;

(b) the application money received by the company for allotment of any securities and due for refund;

(c) matured deposits with the company;

(d) matured debentures with the company;

(e) interest accrued on the amounts referred to in clauses (a) to (d) above; if such amounts have remained unclaimed and unpaid for a period of seven years from the date they became due for payment and filed a copy of challan evidencing such deposit with the Registrar.

(ii) whether company has filed Form I of Investor Education and Protection Fund (Awareness and Protection of Investors) Rules, 2001 duly certified.

(iii) whether the other provisions of Investor Education and Protection Fund Rules, 2001, as far as applicable were complied with.

13. Number and Appointment of Directors

Check whether:

(a) the appointment conforms to the provisions contained in the Articles;

(b) the company has the minimum number of directors - three in the case of a public company and two in the case of a private company;

(c) if the number had fallen below the minimum, whether action was taken to bring the number atleast to the minimum;

(d) if it is a new company, check if the first directors were appointed in accordance with the Articles;

(e) in the case of a public company whether the provisions of Sections 255 and 256 have been duly complied with;

(f) persons other than retiring directors who were candidates for directorship at the general meeting had given not less than fourteen days notice and made a deposit of Rs. 500/- per candidate and had also complied with the provisions
(g) in the case of a public company if the number of directors has been increased beyond 12, approval of the Central Government under Section 259 has been obtained;

(h) if the Board has filled up casual vacancy among directors appointed in general meeting, the appointment was in accordance with the Articles and was made at a meeting of the Board;

(i) if the Board has appointed any alternate/additional director during the year under Sections 313 and 260 respectively, the appointment was in accordance with the Articles;

(j) if any nominee director has been appointed during the year, the appointment is in consonance with the provisions of the Articles of the company;

(k) the company has complied with the provisions of Section 265 where it has adopted principle of proportional representation for appointment of directors;

(l) in the case of a public company, check whether it has secured Central Government approval as required under Section 268 for amendment of any provision relating to the appointment or re-appointment of managing or wholetime director or of a director not liable to retire by rotation;

(m) directors other than those referred to in Sub-section (2) of Section 264 had given consent to act as director within 30 days of his appointment and the consent was filed with the ROC as an attachment in Form No. 32;

(n) none of the directors suffers from any of the disqualifications with reference to Section 274 and Companies (Disqualification of Directors under section 274(I)(g) of the Companies Act, 1956 Rules, 2003 and a form DD-A had been filed by the director(s) before appointment/reappointment. [If the director is disqualified, the auditor should have reported the same to the members and the company should have filed e-form DD-B with the Registrar of Companies]. Also, whether any application has been filed in e-form DD-C for removal of disqualification of directors;

(o) none of the directors is holding directorships in more than 15 companies subject to provisions of Section 278 of the Act;

(p) the office of any director stands vacated on account of any of the disqualifications specified in Section 283 or contravention of the provisions of Section 314(1);

(q) the Board has taken note of the resignation tendered by any director or has accepted the same in terms of articles;

(r) the company has filed form No. 32 for any change among directors/managing director;

(s) in the case of a private company, the office of any director stands vacated on account of any of the additional grounds specified in the Articles of Association;

(t) If any director was removed before the expiry of his term of office, in accordance with the provisions of Section 284 such director was not appointed afresh by the Board of directors as per proviso to Section 284(6);
and

(u) whether Register of Directors (Section 301) and Register of Directors Shareholdings (Section 307) have been maintained.

14. Appointment of Managing Director, Whole-time Director or Manager

Check whether:

(i) the appointment conforms to provisions contained in the Articles of Association;

(ii) the appointment was made in accordance with the provisions Section 269;

(iii) appointment had been made pursuant to Schedule-XIII (a) the appointee has furnished a declaration or otherwise stated that he satisfies the conditions specified in Part I of Schedule XIII; (b) the appointment was in accordance with the conditions specified in Schedule XIII; (c) return in e-Form No.25C was filed with the Registrar within 90 days of the date of appointment; (d) the appointment had been approved by the members in general meeting; (e) in case of appointment of managing director, e-Form No. 23 was filed with the ROC within 30 days; (f) e-Form No. 32 has been filed; and (g) in case the appointee had not completed the age of 25 years, but had attained the age of majority or had attained the age of 70 years, his appointment had been approved by a special resolution and e-Form No. 23 was filed with the ROC; (h) the appointment has been in accordance with the Part II of Schedule XIII i.e. approval of remuneration committee etc. as the case may be.

(iv) an abstract of appointment and remuneration was sent to members of the company within 21 days of appointment under Section 302 of the Act.

(v) the appointment required the approval of the Central Government; if so whether application in e-Form No. 25A seeking the approval of the Central Government was made within ninety days of the appointment and whether the approval of the Central Government has been received;

(vi) the managing director or whole-time director does not suffer from any of the disqualifications specified in Sections 274 and 267. In the case of manager, check with reference to Section 385;

(vii) remuneration paid to Managing/Whole-time Director/Manager is in accordance with the provisions of the Act and terms and conditions of approval;

(viii) the provisions of Section 316/386 where applicable, have been complied with.

(ix) The company had no/inadequate profits, it has paid remuneration etc. according to amended Part II of Section II of Schedule XIII and Remuneration Committee have been formed accordingly.

(x) The company is notified by Department of Commerce as one in special Economic Zones, remuneration not exceeding Rs. 2,40,00,000 per annum or Rs. 2,00,000 per month is paid. Also, provided such companies have not raised
any money by public issue of shares/debentures in India and have not defaulted in India in repayment of any debts including public deposits or debentures or interest thereon for a continuous period of thirty days in a financial year.

15. Appointment of Sole Selling Agents

Check whether:
(i) the company has complied with provisions of Section 294 for appointment of sole selling agents and verify that such appointment is not prohibited under Section 294AA;
(ii) e-Form No. 23 has been duly filed;
(iii) the agreement/resolution states specifically that the appointment shall cease to be valid if it is not approved by the company in the first general meeting held after the date on which appointment is made;
(iv) Central Government required the company to furnish to it information regarding terms and conditions of the appointment of sole selling agent and if so verify whether necessary information was furnished;
(v) the Central Government varied the terms and conditions of sole selling agent and if so whether the same were complied with;
(vi) e-form I has been filed for obtaining approval of Central Government for appointment of sole selling agents;
(vii) such previous approval of the Central Government has been obtained where the individual firm or body corporate appointed as sole selling agent had substantial interest in the company;
(viii) approval by special resolution and of the Central Government was obtained for appointment of sole selling agent where the paid-up share capital of the company was Rs. 50 lakhs or more.

16. Disclosure of interest by the Directors to the Board of Directors

Check whether:
(i) every director has disclosed his interest at the Board meeting where transaction is considered in which he is directly or indirectly interested;
(ii) the notices of disclosure of general interest under Section 299 if received from any director in Form No. 24AA in the last month of the financial year has been placed before and read at the next Board meeting;
(iii) entries thereof have been made in the register under Section 301, (Register of Contracts) noted by the Board;
(iv) such notice under Section 299 if not given at the meeting of the Board, whether it was brought up and read at the meeting of the Board next after it was given;
(v) any director who has been appointed as director of another company during the year has made disclosure thereof in terms of Section 305 of the Act.

17. Issue of Capital and Securities

(a) In Case of Private Companies
Check whether:

(i) the relevant provisions in Articles of Association have been complied with and the increase is within the authorised capital of the company;

(ii) the company has issued equity share capital with differential rights as to dividend, voting or otherwise, if any, in accordance with the Rules prescribed by the Central Government;

(iii) return of allotment was filed with the ROC in e-Form No. 2 in accordance with the provisions of Section 75;

(iv) the register of shareholders/members has been properly maintained and the number of shareholders are not more than 50;

(v) share certificates, have been issued to the allottees in accordance with the Companies (Issue of Share Certificates) Rules, 1960 within the prescribed period; and

(vi) where the company has issued preference shares, provisions of Sections 80(5A) and 80A have been complied with;

(vii) the company has privately placed debentures and if so it has complied with provisions of Section 117C and a copy of the Trust Deed has been forwarded on payment of requisite fee to any member or debentureholder;

(viii) the company, which has completed a buy-back of its shares or other specified securities has not made further issue of the same kind of securities in the last 6 months beginning therefrom, as stipulated in Section 77A(8).

(b) In Case of Public Companies

Check whether:

(i) at the first instance the shares are offered to the existing shareholders in proportion to the capital paid-up on shares held;

(ii) in case shares are offered to any persons whether or not those persons include existing shareholders in any manner whatsoever:

(a) special resolution was passed; or

(b) else the votes cast in favour of the resolution exceeded the votes cast against the proposal and the approval of the Central Government was obtained;

(c) in case of special resolution, e-Form No. 23 was filed with the ROC;

(d) in case of Public Issue, separate Bank Accounts have been opened and whether Board resolutions have been passed.

(iii) the company has issued equity share capital with differential rights as to dividend, voting or otherwise, if any, in accordance with the Rules prescribed by the Central Government Companies (Issue of Share Capital with Differential Voting Rights) Rules, 2001;

(iv) the Board has approved the draft prospectus/letter of offer of rights/offering circular (restricting circulation to below 50 persons) before issue;

(v) the appointments of all the agencies dealing with the issue were duly
approved by the Board;

(vi) initial listing application/s has/have been filed with the Stock Exchanges before filing the prospectus with the ROC;

(vii) minimum subscription has been raised;

(viii) the company has received the minimum subscription in terms of guidelines issued in this regard;

(ix) the basis of allotment has been approved by the Regional Stock Exchange;

(x) in the case of listed companies permission for listing of securities has been received from all the Stock Exchanges mentioned in the prospectus.

(xi) refund orders were sent in time;

(xii) listing agreements were signed with the Stock Exchanges where the shares were to be listed and the executant on behalf of the company had the authority from the Board and whether listing/trading permissions have been obtained;

(xiii) in case debentures have been issued with an option to convert whole or part into shares, check the applicability of the Public Companies (Terms of Issue of Debentures and Raising of Loans with Option to Convert such Debentures and Loans into Shares) Rules, 1977;

(xiv) the company which has completed a buy-back of its shares or other specified securities has not made further issue of the same kind of securities in the last 6 months as stipulated in Section 77A(8);

(xv) the provisions of SEBI (Disclosure and Investor Protection) Guidelines, 2000 have been complied with.

(c) Preferential Issue by Listed Companies

Check whether listed company has issued capital by way of shares/FCDs/PCDs or any other financial instruments on a preferential basis which would be converted into or exchanged with equity shares at a later date to any select group of persons. If yes, then—

(i) check that the issue was not offered to more than 50 persons in conformity with Sub-section (3) of Section 67;

(ii) in case shares are offered to any persons whether or not those persons include existing shareholders in any manner whatsoever:

(a) special resolution was passed; or

(b) else the votes cast in favour of the resolution exceeded the votes cast against the proposal and the approval of the Central Government was obtained;

(c) in case of special resolution, Form No. 23 was filed with the ROC.

(iii) Check whether the provisions of SEBI guidelines in this regard have been complied with.

(d) Issue of Debentures

Check whether:

(i) the company has appointed one or more debenture trustees before issue of
prospectus or letter of offer to the public for subscription of its debentures;
(ii) the debenture trustee does not suffer from any of the disqualifications with reference to the provisions of proviso to Section 117B(1);
(iii) the company has stated on the face of such prospectus or letter of offer that the trustees have given their consent;
(iv) a Trust Deed has been executed within such period and in such form as prescribed for securing any issue of debentures (Section 117A);
(v) a copy of Trust Deed is made available for inspection to any member or debenture holder;
(vi) a copy of the Trust Deed has been forwarded on payment of requisite fee to any member or debentureholder;
(vii) the company has complied with the Order of the Company Law Board, if any, with regard to incurring of any further liabilities;
(viii) the company had re-issued the redeemed debentures in accordance with Section 121; if so, check that such re-issue was not prohibited by companys Articles, in the conditions of issue or in any contract entered into by the company or the company has manifested its intention that the debentures shall be cancelled.
(ix) A public company which has issued debentures after the commencement of Companies (Amendment) Act, 2000 is required to create a debenture redemption reserve out of its profits, for redemption of debentures. Also SEBI guidelines in this respect have to be followed.
(x) the provisions of SEBI (DIP) Guidelines, 2000 have been complied with.

(e) Issue of Sweat Equity Shares

Check whether:
(i) at least one year has elapsed since the date on which the company was entitled to commence business;
(ii) that the sweat equity shares issued are shares only of a class already issued;
(iii) that a special resolution was passed at a general meeting authorising the issue;
(iv) also that the special resolution specified the number of shares, current market price, consideration, if any, and the class or classes of directors or employees to whom such shares are to be issued;
(v) whether the company has filed e-Form No. 23 with the ROC along with a copy of the resolution within 30 days from the date the resolution was passed;
(vi) if the company is an unlisted company, that the issue of sweat equity shares was in accordance with the rules as prescribed by the Central Government, Unlisted Companies (Issue of Sweat Equity Shares) Rules, 2000.

If the Company is a Listed Company

Check inter alia :
(vii) the company had forwarded 3 copies of the notice and one copy of the
proceedings of the general meeting to the stock exchange;

(viii) that the issue was in accordance with the regulations made by SEBI in this regard;

(ix) if the shares were issued for consideration other than cash, the Articles of the company permit the same.

(g) Issue of Shares with Differential Voting Rights

Check that:

(i) the Articles of Association authorizes the issue of shares with differential voting rights;

(ii) the company has not been convicted of any offence arising under the SEBI Act, 1992; Securities Contracts (Regulation) Act, 1956 or the Foreign Exchange Management Act, 1999;

(iii) the company had distributable profits in terms of section 205 of the Act during the three financial years preceding the year in which aforesaid shares were issued;

(iv) the company has not defaulted in filing annual accounts and annual returns during the immediately preceding three financial years preceding the financial year in which the aforesaid shares were issued;

(v) the company has not failed to repay its deposits or interest thereon on due date or redeem its debentures on due date or pay dividend after it was declared;

(vi) the provisions in the Memorandum allow issue of the said shares. If not, whether the proposal for issue of the said shares. If not, whether the proposal for issue of the said shares has been approved by the shareholders under section 94 of the Act;

(vii) the company has not defaulted in meeting investors’ grievances;

(viii) the proposal for issue of the said shares has been approved by the shareholders by special resolution by Postal ballot in the case of a listed company and by the shareholders of any other company by special resolution under section 81 of the Act;

(ix) the sum total of the shares issued with differential voting rights is not more than 25% of the total capital of the company;

(x) the explanatory statement relating to the said resolution sets out the—

(a) the rate of voting right which the equity share capital with differential voting right shall carry;

(b) the scale or in proportion to which the voting rights of such class or type of shares will carry;

(c) the company shall not convert its equity capital with voting rights into equity share capital with differential voting rights and the shares with differential voting rights into equity share capital with voting rights;

(d) the shares with differential voting rights shall not exceed 25% of the total
share capital issued;

(e) statement that a member of a company holding any equity share with differential voting rights shall be entitled to bonus shares, right shares of the same class;

(f) the holders of the equity shares with differential voting rights shall enjoy all other rights to which the holder is entitled to except right to vote as indicated in (a) above.

(xi) a register of members of shares with differential voting rights is being maintained.

(f) **Capitalisation of Profit/Issue of Bonus Shares**

Check whether:

(i) Articles of Association of the company provide for capitalisation of profits;

(ii) requisite resolution was passed by the shareholders in their meeting for capitalisation of profits and issuing bonus shares;

(iii) bonus issue is made out of free reserves built out of genuine profits or share premium collected in cash only and reserves created by revaluation of fixed assets are not capitalised;

(iv) return of allotment in e-Form No. 2 was filed within 30 days of passing resolution.

In the Case of Listed Company, also check whether:

(v) guidelines issued by SEBI relating to Bonus shares for disclosure and investor protection have been duly complied with;

(vi) issue of bonus shares is not made prior to 12 months after a public/right issue;

(vii) the bonus proposal has been implemented within six months from the date of Board’s approval.

18. **Buy-Back of Shares/Securities**

If the company has bought back any shares/securities, check whether:

(i) the Articles authorise buy back of securities;

(ii) a special resolution was passed at a general meeting approving the buy-back of securities and the same was filed along with e-Form No. 23 with the ROC within 30 days from the date of passing the resolution;

(iii) the buy-back was made only out of the company’s free reserves, securities premium account, the proceeds of any shares or other specified securities;

(iv) the buy-back was not made out of the proceeds of an earlier issue of the same kind of shares/securities;

(v) (a) the aggregate value of buy-back was not exceeding 25% of the total paid-up capital and free reserves of the company.

(b) if the buy-back was of equity shares in the financial year, it did not
exceed 25% of the total paid-up equity capital in that financial year.

(c) all the shares/securities so bought back were fully paid-up.

(d) the ratio of debt including all amounts secured and unsecured owed by
the company was not more than twice the capital and its free reserves
after such buy-back, except where a higher ratio has been prescribed by
the Central Government for a class or classes of companies.

(vi) Notwithstanding the provisions of Section 77A(2) in case buy-back was upto
10% of total paid-up equity capital and free reserves of the company, the
same has been authorised by the Board by means of a resolution passed at
its meeting [Proviso to Section 77A(2)].

Provided no offer of buy-back was made within a period of 365 days
reckoned from the date of the preceding offer of buy-back, if any.

(vii) the buy-back process was completed within 12 months from the date of
passing of the special resolution; if it was not completed within the stipulated
time also check whether the reasons thereof were stated in the Board's
report;

(viii) If the Company is an Unlisted Public Limited Company or a Private Limited
Company, Check whether:

(a) the buy-back was made in accordance with the Private Limited Company
and Unlisted Public Limited Company (Buy-back of Securities) Rules,
1999 issued by the Department of Company Affairs;

(b) the company had passed a special resolution and an explanatory
statement was annexed to the notice containing disclosures as specified
in Schedule I to the Rules;

(c) a draft letter of offer containing particulars specified in Schedule II to the
Rules was filed with ROC;

(d) a declaration of solvency in e-form 62 (form No. 4A) was filed with the
ROC along with the letter of offer;

(e) the letter of offer was despatched immediately after filing with ROC but
not later than 21 days from its filing with ROC;

(f) the offer for buy-back remained open to the members for a period not
less than 15 days and not exceeding 30 days from the date of despatch
of letter of offer;

(g) the acceptance per shareholder was on proportionate basis where
shares offered by shareholders are more than the total number of shares
to be bought back;

(h) the company had immediately after the date of closure of the offer
opened a special bank account and deposited therein such sum, as
would make up the entire sum due and payable as consideration for the
buy-back in terms of the Rules;

(i) the share certificates so bought back were extinguished and physically
destroyed in the presence of a Practising Company Secretary within 7
days of the last date of completion of buy-back;

(j) the company had furnished with the ROC a certificate duly verified by two
directors including the Managing Director and a Practising Company Secretary certifying compliance with above mentioned Rules and also specifically Rule 10(1) of the said Rules regarding extinguishing of share certificates within 7 days of the extinguishing and destruction of the certificates;

(k) the company has filed with the ROC a return on buy-back of securities as prescribed in Annexure 'A' of the said Rules within 30 days of completion of the buy-back;

(l) the register of buy-back of securities has been maintained by the company as prescribed in Annexure 'B' of the said Rules.

(ix) If the Company is a Listed Company in addition to the requirements stated at (i) to (vii) above check whether:

(a) the buy-back was made as per the SEBI (Buy-back of Securities) Regulations, 1998;

(b) the company has filed with SEBI and the ROC a return on buy-back of securities within 30 days of completion of the buy-back in the prescribed format;

(c) the register of buy-back of securities has been maintained by the company in the prescribed format.

(x) the company which has completed buy-back has not made further issue (including rights issue) of the same kind of shares or other specified securities within 6 months except by way of bonus issues or in the discharge of subsisting obligations such as conversion of warrants, stock option scheme, sweat equity or conversion of preference shares or debentures into equity shares;

(xi) prohibition for buy-back is not attracted in certain circumstances as set out under Section 77B.

19. Redemption of Preference Shares/Debentures

(a) Redemption of Preference Shares

Check whether any preference shares have been redeemed; if so check:

(i) the provisions contained in Articles of Association have been complied with;

(ii) the conditions set out in Section 80 of the Act have been met; and

(iii) e-Form No. 5 has been filed with the ROC within 30 days from the date of redemption.

(b) Redemption of Debentures

Check whether:

(i) company has followed the provisions in the Articles of Association;

(ii) the company has created a debenture redemption reserve for the redemption of debentures and credited adequate amount from out of the profits until such debentures are redeemed;

(iii) the company has not utilised the debenture reserve except for the
redemption of debentures;
(iv) the company has paid interest and redeemed the debentures in accordance with the terms and conditions of their issue;
(v) the company has complied with the order, if any, of the Company Law Board with regard to redemption of debentures.

20. Rights to dividend, rights shares and bonus shares held in abeyance

Check whether:
(i) rights to dividend, rights shares and bonus shares have been held in abeyance in cases where the instrument of transfer has been delivered to the company and the transfer of such shares has not been registered by the company;
(ii) in case instrument of transfer of shares is pending registration with the company, check whether the dividend relating to such shares has been transferred to a special bank account opened by the company under Section 205A unless the company is authorised by the registered shareholder, in writing, to pay such dividend to the transferee specified in the instrument of transfer.

21. Borrowings by Way of Deposits

(a) Borrowings by way of deposits by Private Companies

Check whether—
(i) the company has altered its Articles of Association to include the restrictive provisions under section 3(1)(iii)(d) limiting the sources of deposits and thereafter has accepted the deposits only from such sources.
(ii) the company has accepted deposits from its directors only after obtaining the written declaration as required under Rule 2(b)(ix) of the Companies (Acceptance of Deposits) Rules, 1975.
(iii) the company has accepted deposits from its members only after obtaining the written declaration as required under rule 2(b)(ix) and in case of a non-financial company, whether the concerned depositor has continued to be a member of the company upto 24-9-2001 (Rule 2(b)(ix) amended by the Companies (Acceptance of Deposits) Second Amendment, Rules, 2001) (if a financial company, whether the concerned depositor has continued to remain a member of the company all throughout the term of the deposit and also if he happened to be a joint-member, whether his name appeared first amongst the joint-members).
(iv) the non-financial company has accepted deposits from any of the relatives of its directors upto 24-9-2001 and if yes, whether the company has delivered to ROC before accepting such deposits, the Statement in lieu of advertisement under rule 4A of the Rules.
(v) the company has accepted any deposits from other sources exempted under rule 2(b) of Deposit Rules in conformity with the stipulations thereunder.
(vi) the company has accepted any deposits in pursuance of the exemption
granted to Small Scale Industrial Units and if yes, whether the conditions specified in respective Notification i.e., G.S.R. No. 73(E) dated 2-2-1996 have been duly fulfilled.

(vii) the company has accepted any deposits prior to 13-12-2000 [Date of commencement of the Companies (Amendment) Act, 2000] in conformity with section 58A and Deposit Rules and if yes, whether in respect of any outstandings thereof, the company has filed the Return of Deposits with ROC before 30th June with a copy to RBI.

(b) Borrowings by way of Deposits by NBNFCs

Check whether:

(i) the net owned fund of public company investing deposit is not less than rupees one crore;

(ii) the company is not in default in the repayment of any deposit or part thereof and any interest thereupon in accordance with the terms and conditions of such deposit;

(iii) approval of the Board in terms of Section 292(1) has been obtained to invite deposits and draft advertisement has been approved;

(iv) the advertisement has been issued on the authority and in the name of the Board;

(v) the advertisement contains the particulars specified in Rules 4(2) (a) to (k) of the Companies (Acceptance of Deposits) Rules, 1975. In case deposits were accepted without invitation, check that a statement in lieu of advertisement has been delivered to the ROC before accepting deposits (Rule 4A);

(vi) a copy of the advertisement duly signed by majority of directors was filed with the ROC, for registration, before publishing the same;

(vii) advertisement has been published in a leading English newspaper and one vernacular newspaper circulating in the State where the registered office is situated within the 90 days;

(viii) proper scrutiny of the fixed deposit application forms, particularly the name(s), amount, address and other relevant particulars, has been done;

(ix) no deposits were accepted which were repayable on demand or notice for a period of less than six months and more than three years;

(x) deposits have been accepted within the limits prescribed in Rule 3(2);

(xi) the rate of interest on deposits is within the prescribed limit;

(xii) the rate of brokerage is within the prescribed limits;

(xiii) the company, deposits/invests on or before 30th April of each year not less than the prescribed limit of the deposits maturing during the year, in specified securities (Rule 3A);

(xiv) proper receipts were issued to the depositors on the acceptance of deposits;

(xv) register of deposits has been maintained with particulars specified in Rule 7;

(xvi) return of deposits duly certified by the auditor of the company has been filed
with the ROC and Reserve Bank of India on or before 30th June giving the position as on 31st March;

(xvii) payment of interest has been made on time;

(xviii) deposits were repaid on time. In case of repayment of deposits before maturity, the company has complied with the requirements of the Rules in this regard;

(xix) where the company has obtained any extension of time or exemption under Section 58A(8), the terms thereof have been complied with;

(xx) in case any order has been made by the Company Law Board under Section 58A(9), it has been complied with;

(xxii) the company has complied with applicable directions issued by RBI, if any;

(xxii) penal rate of interest, as prescribed, has been paid for the overdue period.

(c) Borrowings by ways of Deposits by NBFCs

Check whether:

(i) the company having Net Owned Fund of one crore of rupees and above, has obtained minimum investment grade or other specified credit rating for fixed deposits from any one of the approved credit rating agencies at least once a year;

(ii) the copy of rating as specified above, has been sent to the Reserve Bank of India along with return on prudential norms;

(iii) the company has informed the Reserve Bank of India, about upgrading or down grading of its credit rating to any level from the level previously held by it, within fifteen working days of its being so rated;

(iv) no deposits were accepted or renewed for a period less than twelve months and more than sixty months from the date of acceptance or renewal thereof;

(v) the company has complied with the provisions of Non-Banking Financial Companies and Miscellaneous Non-Banking Companies (Advertisement) Rules, 1977;

(vi) the company has delivered to RBI, a statement in lieu of advertisement containing all particulars required to be included in the advertisement pursuant to NBFC and Miscellaneous Non-Banking Companies (Advertising) Rules, 1977 and complied with other requirements of para 13 of NBFCs Acceptance of Public Deposits (Reserve Bank) Directions, 1998;

(vii) the rate of brokerage is within the prescribed limits;

(viii) the rate of interest on deposits is within the prescribed limits;

(ix) no deposits were accepted or renewed which are repayable on demand;

(x) register of deposits has been maintained and particulars specified in para 16 of NBFCs Acceptance of Public Deposits (Reserve Bank) Directions, 1998 have been entered therein;

(xi) deposits were repaid in time. In case of repayment of deposits before maturity, the company has complied with the provisions of para 14 of NBFCs Acceptance of Public Deposits (Reserve Bank) Directions, 1998;

(xii) proper receipts were issued to the depositors on the acceptance of deposits;
(xiii) no public deposits were repaid within a period of three months from the date of its acceptance;

(xiv) the company has complied with the provisions of para 9 of NBFCs Acceptance of Public Deposits (Reserve Bank) Directions, 1998 for permitting an existing depositor to renew the deposit before maturity for availing of benefit of higher rate of interest.

(xv) the company has complied with the provisions of para 12 of NBFCs Acceptance of Public Deposits (Reserve Bank) Directions, 1998 regarding particulars to be specified in application form soliciting public deposits;

(xvi) the company has complied with the provisions of para 10 of NBFCs Acceptance of Public Deposits (Reserve Bank) Directions, 1998 for payment of interest on overdue public deposits;

(xvii) if the company is an equipment leasing company or a hire purchase finance company, it has complied with the provisions of para 4(4)(a) & (b) and para 5 of NBFCs Acceptance of Public Deposits (Reserve Bank) Directions, 1998 for acceptance or renewal of deposits;

(xviii) if the company is loan company or an investment company, it has complied with the provisions of para 4(4)(c), (d) & (e) and para 5 of NBFCs Acceptance of Public Deposits (Reserve Bank) Directions, 1998 for acceptance or renewal of deposits.

(d) Deposits from Small Depositors

Where the company has accepted deposits from small depositors as defined under Section 58AA and has made any default in repayment of any such deposits or part thereof or interest thereupon check whether:

(i) the company has sent an intimation of default, if any, in repayment of deposit or part thereof or interest thereupon to the Company Law Board within 60 days from the date of default on monthly basis;

(ii) the intimation includes the particulars in respect of names and addresses of each small depositor, the principal sum of deposits due to them and interest accrued thereupon;

(iii) the company has complied with the order of the Company Law Board, if any;

(iv) the company has not accepted further deposits from small depositors unless each small depositor, whose deposit has matured has been paid the amount of deposit and the interest accrued thereupon. This condition shall not apply if deposit is renewed by the small depositor voluntarily or repayment thereof has become impracticable or been stayed by a competent court or authority;

(v) the company has stated in every advertisement and application form inviting deposits from the public issued after the default, the total number of small depositors and amount due to them in respect of which such default had been made;

(vi) the company has mentioned in the advertisement and application form inviting deposits issued by it after the default the fact of waiver of interest accrued on deposits of the small depositors, if any;
(vii) the company has after default taken a loan for the purpose of working capital from any bank, whether the company has first utilised the funds so obtained in repayment of any deposit or any part thereof or any interest thereupon to the small depositors before applying such funds for any other purpose;

(viii) the application form, issued by the company to small depositors for accepting deposits from them, contained a statement that the applicant had been apprised of:
   — every past default
   — the waiver of interest and reasons therefor.

22. Borrowing Powers

(a) In Case of Private Company

Check whether there are any restrictions on the amount of borrowings contained in the Articles of Association of the company. If yes, check whether borrowings are in accordance with the provisions contained in the Articles.

(b) In Case of Public Company

Check whether:

(i) the Memorandum and Articles contains provisions with respect to the powers of the company to borrow money and to charge the assets of the company;

(ii) the power to issue debentures has been exercised at the meeting of the Board;

(iii) the power to borrow money, otherwise than on debentures, has been exercised at the meeting of the Board;

(iv) the power to borrow money otherwise than on debentures has been delegated to a committee of directors or managing director or manager or any other principal officer of the company or in the case of a branch office principal officer of the branch office, if the delegation was made at the meeting of the Board and the resolution delegating the power specified the total amount outstanding, at any time, up to which the money may be borrowed by the delegate;

(v) the total amounts borrowed (apart from temporary loans obtained from the company’s bankers in the ordinary course of business) exceed the aggregate of the paid-up capital of the company and its free reserves, if so, consent of the members in general meeting has been obtained. Verify the resolution passed by the shareholders and the total amount specified therein up to which moneys may be borrowed by the directors;

(vi) Form No. 23 has been filed with the ROC under Section 192(4)(ee)(i).

23. Loans, Investments, Guarantees and Securities (Section 372A)

(a) Check whether provisions of Section 372A are applicable [refer Section 372A(8)]. If provisions of Section 372A are applicable, check whether the aggregate of the loans made, guarantees given, securities provided or
Investments made by the company are within the limits prescribed under Section 372A.

(b) Check that:

(i) the company has not defaulted in complying with the provisions of Section 58A;

(ii) Board resolutions were passed with the consent of all the directors present at the meeting;

(iii) the details regarding the transaction were entered chronologically in the Register maintained in this regard as per the provisions of Section 372A(5), within 7 days of the transaction(s); and

(iv) the company has obtained prior approval of the public financial institutions, where any term loan is subsisting if it has defaulted in repayment of loan instalments or payment of interest thereon as per terms and conditions of such loan.

(c) If the aggregate has exceeded the prescribed limits, check whether:

(i) Board resolutions were passed unanimously approving the impending transaction subject to members' previous approval at general meeting;

(ii) the company has secured prior approval of the public financial institutions where any term loan is subsisting as required under Sub-section (2) of Section 372A;

(iii) general meeting(s) (AGM or EGM) have been held and specific special resolutions have been passed stating the limits, particulars of body(ies) corporate in which the investment is proposed to be made or loan or security or guarantees to be given, the purpose and the specific source of funding etc.;

(iv) In case of listed companies, the resolution was passed through postal ballot process;

(v) no omnibus special resolution(s) have been passed;

(vi) in the case of guarantees given by the Board of directors without the authorisation of special resolution(s) check that:

— exceptional circumstances existed which prevented the company from obtaining the resolution;

— the Board passed a resolution authorising the same in accordance with the provisions of Section 372A;

— the Board resolution has been confirmed within 12 months at the earliest general meeting of the company;

— notice of such general meeting (whether annual or extra-ordinary) indicated clearly the specific limits, the particulars of body(ies) corporate for which the guarantee was given etc.

(d) in the case of loans, check whether the interest rate at which it was made
was not lower than the prevailing bank rate as prescribed under Section 49 of the Reserve Bank of India Act, 1934;

(e) the details regarding the transaction(s) were entered chronologically in the register maintained in this regard as per the provisions of Section 372A(5), within 7 days of the transaction(s).

24. Memorandum of Association

*Alteration in the memorandum of association with respect to change in registered office from one state to another and object clause*

(i) Check whether:

(a) the Board of directors had passed a resolution for change in registered office of the company/alteration of object clause;

(b) the Board has called a general meeting and necessary special resolution has been passed at the said meeting;

(c) a certified true copy of the special resolution along with the certified true copy of the explanatory statement was filed with the Registrar in Form No.23, within thirty days from the date of passing of the resolution;

(d) a petition has been filed before the Company Law Board, for confirmation of the alteration of Memorandum relating to change of place of the company's registered office from one State to another.

(e) a certified true copy of the order of the CLB confirming the Alteration of memorandum in respect of registered office of the company together with the printed copy of the Memorandum as altered was filed with the ROC of each State;

(f) the Registrar of each State registered the same and issued the Certificate of registration under his hand; and

(g) every copy of the memorandum issued after the date of alteration is in accordance with the alteration.

*Shifting of registered office from a place under the jurisdiction of one ROC to a place under the jurisdiction of another ROC within the same state*

(ii) Check whether:

(a) the company has passed a special resolution in the general meeting for shifting its registered office from a place under the jurisdiction of one ROC to a place under the jurisdiction of another ROC, within the same State;

(b) it has made application in form 1AD to the Regional Director for confirmation of special resolution;

(c) the RD had passed the confirmation order of the resolution within four weeks from the date of receipt of the company’s application;

(d) the company has filed with the ROC, from whose jurisdiction it proposes to shift the registered office, a copy of the confirmation order of the
Regional Director along with the printed copy of the memorandum as altered within 2 months from the date of confirmation by the Regional Director; and

(e) the ROC from whose jurisdiction Registered Office has been shifted, has registered the documents and certified the registration under his hand within one month from the date of filing of such documents.

(iii) Check whether the provisions of the Memorandum with respect to the objects of the company was altered during the year. If so, check whether:

(a) the company has filed with the ROC in Form No. 23 the special resolution passed by the company within one month from the date of such resolution;

(b) the ROC issued certificate registering alterations; and

(c) the alterations had been incorporated in all the copies of the Memorandum.

(d) the resolution was passed through postal ballot process and the alteration was notified to the Stock Exchange if the shares were listed.

Name and Capital

(iv) Check whether the company changed its name during the year. If so, check whether:

(a) the company had obtained the availability of new name from Registrar or Companies;

(b) the Board of Directors had called and held the general meeting within six months of date of intimation from Registrar;

(c) the company has passed a special resolution and filed eForm No. 23 with the ROC within 30 days and obtained Central Governments approval where applicable;

(d) fresh certificate of incorporation was obtained from the ROC;

(e) the name has been painted/affixed/printed on the name board, business letters, bill heads, Memorandum and Articles;

(f) new common seal has been adopted by the Board; and

(g) the change was notified to Stock Exchanges if the shares are listed.

(v) Check whether the company altered the conditions of its Memorandum as regards share capital in any of the ways mentioned in Section 94(1). If so, check whether:

(a) alteration was authorised by the Articles and the general meeting;

(b) alteration had been effected in all copies of Memorandum and Articles etc.; and

(c) e-Form No. 5 and 23 were filed with the ROC within 30 days.

(d) the alteration was notified to the stock exchange if the shares were listed.

(e) every copy of the memorandum and articles issued after the date of alteration is accordance with alteration.
25. Articles of Association

(a) Check the extent of applicability of Table A of Schedule I of the Act.

(b) Check whether the articles were altered during the year under Section 31. If so, check whether:

   (i) copy of the special resolution was filed with the Registrar in Form No. 23;
   (ii) the change had been incorporated in all copies of the articles;
   (iii) if the alteration had the effect of converting a public company into a private company, whether:
       — approval of the Registrar of Companies was obtained; and
       — a printed copy of the articles as altered was filed with the Registrar within one month of the date of the receipt of the order of approval; and
       — In case shares of the company were listed on a recognised Stock Exchange, the resolution was passed through postal ballot process;
   (iv) the alteration has been notified to the stock exchange in case the shares are listed.

26. Prosecution or Show Cause Notices

Check whether:

   (i) ROC has issued any show-cause notice for non-compliance of any provision of the Act. Verify the explanations given in the light of alleged default.
   (ii) The Board considered the show cause notice at a meeting or otherwise.
   (iii) Any inspection or investigation into the affairs of the company has been ordered and whether it is outstanding at the time of issue of the certificate.
   (iv) Any penalty, fine or punishment has been imposed on the company and whether it has been complied with.

27. Deposit of Employees Security Deposits

Check whether:

   (i) any money or security deposited with the company by any employee in pursuance of his contract of service with the company has been kept or deposited by the company within 15 days from the date of deposit in an account as specified in Clauses (a) to (c) of Sub-section (1) of Section 417;
   (ii) the company has not utilised any portion of such money or securities except for the purposes agreed to in the contract of service.

28. Deposit of Contribution to Provident Fund

Check whether:

   (i) the company has constituted a Provident Fund for its employees or any class of employees. If yes, check that all moneys contributed to such fund (whether
by the company or by the employees) or received or accruing by way of interest or otherwise to such fund has been deposited within 15 days from the date of contribution, receipt of accrual, as the case may be, in an account as specified in clause (a) of Sub-section (1) of Section 418 or invested in the securities mentioned or referred to in clause (a) to (e) of Section 20 of the Indian Trust Act, 1882.

(ii) where the company has created a trust for the employees provident fund, the company shall collect the contribution and pay to the trustees of the said fund, the employees' and employer's contributions within 15 days from the date of collection. Also, the Board for this purpose shall approve the execution of trust deed, appointing trustees, getting approval of commissioner of Income-tax etc.

(iii) if the employees' contribution is deducted from their salary, verify the amount deducted from salary register.

(iv) the employees' contribution is equal to the employer's contribution and aggregate tallies with the quantum mentioned in the statement sent to Provident Fund Commissioner.

CHECK LIST FOR OTHER COMPLIANCES

There may be certain matters which have bearing on the compliances under the Companies Act although not directly referred to in the 33 paragraphs of the Form appended to the Companies (Compliance Certificate) Rules, 2001. An illustrative but not exhaustive list of some such matters is given below. It is likely that PCS during the course of scrutiny comes across non-compliance with regard to such matters. While PCS need not qualify non-compliance of such matters he/she may suitably advise the management on the same.

1. DIRECTORS/OFFICERS

   (a) Appointment of Officers

   Check whether:

   (i) the company has appointed qualified secretary in conformity with section 2(45) and 383A read with the Companies (Appointment and Qualifications of Secretary) Rules, 1988 and filed Form No. 32 with Registrar of Companies within 30 days from the date of appointment;

   (ii) the company has charged any person with the responsibility of complying with specified provisions as per section 5 and if so whether Form Nos. 1AA, 1AB and 1AC as the case may be under the Companies (Central Government’s) General Rules and Forms, 1956 have been filed with ROC within 30 days;

   (iii) if receiver or manager of property of the company under section 137 has been appointed, notice thereof has been given to the ROC within 30 days in Form No. 15 of the Companies (Central Government’s) General Rules and Forms, 1956;

   (iv) in case company has appointed a Manager, it has complied with the provisions of section 269 of the Act read with Schedule XIII.
(b) **Vacation of Office of Directors**

Check whether:

(i) the director has vacated his office on happening of any of the events specified under section 283(1) of the Act;

(ii) the director has vacated his office on account of any contraventions of sections 314(1) and 314(1B);

(iii) in case of a private company, the director has vacated his office on any other ground as specified in the Articles in addition to those specified in sub-section (1) of section 283.

(c) **Retirement of Directors**

Check whether:

(i) one third of such directors for the time being as are liable to retire by rotation, or if their number is not three or a multiple of three, then, the number of nearest to one third, retire from office at first annual general meeting and at every subsequent annual general meeting;

(ii) the directors retiring by rotation are those who have been longest in office since their last appointment;

(iii) between directors appointed on the same day, the retirement was, in default of and subject to any agreement among themselves, determined by draw of lots;

(iv) the company has filled up such vacancy by appointing the retiring director or some other person;

(v) the director has stated his willingness for his reappointment;

(vi) the vacancy was filled up at the adjourned meeting, or the retiring director was deemed to be reappointed under provisions of section 256(4).

**Note:** Unless otherwise specified in the Articles of Association, the aforesaid requirements shall not apply to a private company.

(d) **Removal of Directors**

Check whether:

(i) a special notice as required under sub-section (2) of section 284 was given to the company to remove a director;

(ii) the company has sent forthwith a copy thereof to the director concerned and the director was provided opportunity to be heard on the resolution at the meeting;

(iii) the representation, if any, made by concerned director has been notified to the members on the request of the director along with the notice of the resolution and if a copy of the representations was not sent because they were received too late or because of company’s default, it was read out at the meeting on the request of the director;

(iv) the director who was removed from office was not reappointed as a director by the Board of directors;
(v) the company has filed form No.32 with the Registrar of Companies within 30 days from the date of removal;
(vi) any order was passed by Company Law Board for removal of director.

(e) Disclosures

Check whether the company has made the following disclosures:

(i) the address of its registered office as per Section 147;
(ii) the authorised share capital in its official publications and if yes, subscribed/ paid-up share capital as per Section 148;
(iii) directors’ interest in contract(s) appointing manager or managing director as per Section 302.

Check whether the company has complied with the requirements in pursuance of disclosures by directors regarding:

(i) particulars of directors under Section 303;
(ii) particulars of other directorships under Section 305;
(iii) particulars of directorship, membership and partnership under Section 299;
(iv) particulars of directors shareholdings under Section 308;
(v) particulars of interest or concern in any contract under Section 297.

(f) Appointment/Change and Remuneration of Auditors

Check whether:

(i) the appointment and remuneration of auditors are in order with reference to Sections 224, 224A, 225, 226 and 228;
(ii) the company has obtained requisite intimation under Section 224(1B) before appointment/reappointment of auditors;
(iii) the company has intimated appointment/reappointment of auditors under Section 224(1).

(g) Redemption of Irredeemable Preference Shares under Section 80-A

Check whether the company had issued before the commencement of the Companies (Amendment) Act, 1988 preference shares which were irredeemable or not redeemable before the expiry of ten years, if so:

(i) whether steps had been taken to comply with the requirements of Section 80A(1)(a) or 80A(1)(b) as the case may be;
(ii) if the company was not in a position to redeem any such share within the period specified in Clause (a) or (b) of Sub-section (1) of Section 80A, check whether consent of the Company Law Board had been obtained for issue of further redeemable shares equal to the amounts due (including the dividend thereon) in respect of unredeemed preference shares.

(h) Commencement of New Business stated in ‘Other Objects’ in the Memorandum in the Case of Public Companies
Check whether:

(i) a special resolution was passed under Section 149(2A) before commencement of such new business and e-Form No. 23 was filed with the ROC;

(ii) the shareholders approved the resolution by a simple majority, and if so check whether approval was obtained from the Central Government;

(iii) a duly verified declaration by one of the directors or the secretary or, where the company has not appointed a secretary, by a Practising Company Secretary in e-Form No. 20A was filed with the ROC.

(i) Membership of Holding Company

Check whether:

(i) the company is a member of a company which is its holding company;

(ii) the company which is a member of its holding company has been allotted any shares or acquired further shares after it became a subsidiary as such allotment or transfer is void.

(j) Loans by Company for Purchase of its Own or Holding Company’s Shares

Check whether:

(i) the company gave any financial assistance for the purpose of or in connection with purchase of shares in the company or in its holding company;

(ii) the company had given any such financial assistance, it should be ensured that it fell within the exemption under Section 77.

(k) Remuneration of Directors

Check whether:

(i) the payment of remuneration to directors was within the limits provided under Sections 198 and 309 of the Act;

(ii) 'net profit' has been computed in accordance with the provisions of Sections 349 and 350;

(iii) the remuneration paid to managing director/whole-time director was in accordance with the provisions of the Articles, Schedule XIII to the Companies Act, 1956, resolution passed by the shareholders in general meeting and/or approval of the Central Government;

(iv) remuneration paid if any has been recovered in case approval by the Central Government was either not obtained or denied;

(v) special resolution was passed for payment of remuneration by way of commission to directors who are not whole-time/managing directors;

(vi) increase in the remuneration was effected with Central Government’s approval in accordance with Section 310;

(vii) no other remuneration was paid to a director in any other capacity except as
permitted;

(viii) no tax free payment was made;

(ix) compensation for loss of office, if any, has been paid within the limits specified in Sub-section (4) of Section 319;

(x) the amount of remuneration by way of fee for each meeting of the Board of directors or a committee thereof has not exceeded Rs. 5,000/- or such other amount as may be prescribed from time to time.

Note: The aforesaid requirements do not apply to private companies.

(l) Balance Sheet and Profit and Loss Account

Check whether:

(i) balance sheet and profit & loss account has been prepared in the form set out in Part I and Part II of the Schedule VI;

(ii) Central Government’s permission has been received under Section 211(4) for any modifications in relation to any of the requirements as to the matters to be stated in the company’s balance sheet or profit and loss account.

(m) Cost Audit and Appointment of Cost Auditor

Check whether:

(i) there was an order of the Central Government ordering audit of cost accounts of the company;

(ii) Board resolution was passed for appointing a person as cost auditor and whether he was qualified to act as such;

(iii) approval of the Central Government was obtained for the appointment of the cost auditor and the cost auditor was issued appointment order;

(iv) a copy of the cost audit report was received from the cost auditor;

(v) full information and explanations were furnished to the Central Government for any reservations or qualifications contained in the cost audit report;

(vi) any directions were received from the Central Government for circulation of the cost audit report to the members along with the notice of the annual general meeting and, if so, whether the same has been complied with.

(n) General

Check whether:

(i) a company has served documents on a member in conformity with the provisions of Section 53;

(ii) a public company has paid underwriting commission; if so, check whether it has complied with the provisions contained in Section 76 and its Articles of Association;

(iii) the company has complied with the provisions of Section 188 in respect of circulation of members resolutions;

(iv) the company has paid interest out of capital and if so check the payment has
been authorised by its Articles or by a special resolution in as much as with the previous sanction of the Central Government.

(o) **Conversion of a Public Company (other than Section 43A Company) into a Private Company**

Check whether:

(i) the company has received the approval of ROC;

(ii) the company has passed a special resolution authorising the conversion and altering the Articles so as to contain the matter specified in Section 3(1)(iii) and filed the same with the ROC;

(iii) the company has passed a special resolution as required under Section 21 read with Section 13(1)(a) and filed the same with the ROC;

(iv) in case shares of the company were listed on a recognised Stock Exchange, the resolution was passed through postal ballot process;

(v) the company has obtained consent of every creditor to whom the company owes substantial amounts or has issued a public notice in newspapers for conversion of a public company into a private company;

(vi) the company has obtained fresh certificate of incorporation from ROC;

(vii) the alteration of name has also been effected in the Memorandum and Articles of Association, common seal, name board and other documents.

(p) **Conversion of a Private Company (which is a Subsidiary of a Public Company) into a Public Company**

A private company which is a subsidiary of a public company is a public company as per provisions of Sub-clause (c) of Clause (iv) of Sub-section (1) of Section 3. Therefore, check whether:

(i) it has altered its Articles by deleting provisions relating to matters specified in Clause (iii) of Sub-section (1) of Section 3;

(ii) it has altered its Articles for increasing the number of its members to minimum seven;

(iii) it has altered its Article for increasing the number of its directors to at least three directors;

(iv) it has altered other regulations in the Articles which are not applicable to a public company;

(v) it has a minimum paid-up capital of five lakhs rupees or more on or before 12th December 2002 or such higher paid-up capital as may be prescribed;

(vi) it has filed e-Form No. 23 with the ROC and obtained a fresh certificate of incorporation;

(vii) it has filed prospectus/statement in lieu of prospectus with ROC.

(q) **Conversion of a Private Company into a Public Company under Section 44**

Check whether:
(i) the company has increased the number of its directors to minimum three;
(ii) the company has increased the number of its members to minimum seven;
(iii) the company has secured shareholders’ approval by special resolution for deletion of the Article containing restrictive provisions applicable to a private company [vide Section 3(1)(iii)];
(iv) the resolution has been passed through postal ballot process if the shares of the company are listed;
(v) the company has altered other regulations in the Articles which are not applicable to a public company;
(vi) the company has filed e-Form No. 23 with the ROC alongwith the special resolution and explanatory statement;
(vii) the company has filed prospectus/statement in lieu of prospectus with the ROC;
(viii) the company has received a new certificate of incorporation after deleting the word private in its name.

(r) Statutory Meeting/Class Meetings/General Meeting

(i) Statutory Meeting (in case of a Public Company)

Check whether:

(i) the meeting has been held within the period prescribed under Section 165(1);
(ii) notice of meeting and statutory report in e-Form No. 22 duly certified were sent to the members and ROC; and
(iii) other requirements of a general meeting e.g., quorum, notice, preparation and signing of minutes, etc., were complied with.

(ii) Meeting of Class of Shareholders

Check whether:

(i) the meeting has been convened after duly complying with the provisions under relevant Section and Rule 7 of the Companies (Central Government’s) General Rules and Forms, 1956 e.g., for reduction of capital, for variation of rights of shareholders as directed by Court;
(ii) the applicable provisions (e.g. those under Section 102/106) have been duly complied with;
(iii) subject to directions of the Court, requirements relating to notice, attendance, Chairman, quorum, proxy, proxy register/instruments of proxy and conduct of meeting as well as maintenance of minutes of a general meeting have been complied with.

(iii) Meeting of Creditors and Others

Check whether:

(i) the meeting has been convened after duly complying with rule 7 of the Companies (Central Government’s) General Rules and Forms, 1956, the
terms of agreement or the directions of Court/CLB e.g., meetings convened in sections 391/394 or sections 397/398;

(ii) as directed by the Court, requirements relating to notice, attendance, Chairman, quorum, proxy, proxy register/instruments of proxy and conduct of meeting as well as maintenance of minutes of a general meeting have been complied with.

(iv) Passing of Resolutions by Postal Ballot under Section 192A by a Listed Company

Check whether:

(i) the company has passed any resolution by resorting to postal ballot;

(ii) the company has passed the resolution only by postal ballot in respect of following business declared by the Central Government to be conducted by means of a postal ballot:
   — alteration in the object clause of memorandum;
   — alteration of articles of association in relation to insertion of provisions defining private company;
   — buy-back of own shares by the company under sub-section (1) of section 77A;
   — issue of shares with differential voting rights as to voting or dividend or otherwise under sub-clause (ii) of clause (a) of section 86;
   — change in place of registered office outside local limits of any city, town or village as specified in sub-section (a) of section (1) of section 293;
   — giving loans or extending guarantee or providing security in excess of the limit prescribed under sub-section (1) of section 372A;
   — election of a director under proviso to sub-section (1) of section 252 of the Act;
   — variation in the rights attached to a class of shares or debentures or other securities as specified under section 106.

(iii) the company had sent a notice to all the shareholders:
   (a) by registered post acknowledgement due or under certificate of posting and has published an advertisement in a leading English Newspaper and in one vernacular Newspaper circulating in the State in which the registered office of the company is situated, about having dispatched the ballot papers;
   (b) along with a draft resolution explaining the reasons therefor and requesting them to send their assent or dissent in writing on a postal ballot within a period of thirty days from the date of posting of the letter;
   (c) along with a postage pre-paid envelope for facilitating the communication of assent or dissent of the shareholder to the resolution within the said period.

(iv) the appointment of Scrutinizer is in order i.e., w.r.t. board resolution;

(v) postal Ballot papers from the shareholders were received within thirty days
from the date of issue of Notice;

(vi) the Board resolution making the Company Secretary and one of the functional director responsible for the entire Postal Ballot process was delivered to ROC within one week of passing such resolution;

(vii) the company has sent then notice of resolution to be passed by Postal Ballot by Registered post Acknowledgement due or under Certificate of Posting;

(viii) the resolution was passed without modification;

(ix) the resolution passed was assented to by the requisite majority; and

(x) the Register of Postal ballot, Postal Ballot forms and other documents were maintained and preserved till the resolution was given effect to.

3. Observance of Secretarial Standards

Check whether the company has followed the applicable secretarial standards prescribed by the Institute of Company Secretaries of India constituted under the Company Secretaries Act, 1980 (56 of 1980).

4. Sundry Items (General)

(a) Holding Company and Subsidiary Company

Check whether:

(i) if during the year the company has become a ‘holding company’ or ‘subsidiary company’ under section 4 and where the financial year of the subsidiary does not coincide with that of the holding company there should not have been a gap in excess of six months between the financial year of the holding and subsidiary company;

(ii) in such cases the balance sheet of holding company include certain particulars as to its subsidiaries as required under section 212;

(iii) where the holding company was unable to obtain the required information check whether a report in writing to that effect was attached to the balance sheet of the holding company.

(iv) any exemption was obtained from Central Government and if so whether directions given by Central Government were complied with.

(b) Calls on Shares/Debentures

Check whether:

(i) call on shares/debentures was made by the Board of directors by means of resolutions passed at the Board meeting as required under Section 292(1)(a);

(ii) call on shares/debentures complied with the stipulations contained in the Articles of Association;

(iii) the Board of directors approved the rate of interest payable on delayed payment of calls in conformity with the provisions contained in the Articles of Association.

(c) Forfeiture and Re-issue of Shares
(a) Forfeiture

Check whether:
(i) the company has forfeited shares during the year in accordance with provisions contained in the Articles;
(ii) necessary noting/recording has been done in the Register of members and other registers.

(b) Re-issue of Forfeited Shares

Check whether:
(i) the company has reissued the forfeited shares and if so, the re-issue has been done in accordance with the provisions contained in the Articles;
(ii) the aggregate of the amount received on forfeited shares and amount received on the reissue of those forfeited shares was not below the issue price of the original shares which were duly forfeited;
(iii) share certificates have been issued to the allottee(s) and necessary entries made in the Register of members.

Note: There is no need to file return of allotment with ROC for re-issue of forfeited shares.

(d) Further Issue of Capital

Check whether:
(i) the increase is within the authorised capital of the company otherwise authorised capital should be increased accordingly.
(ii) at the first instance shares are offered to the existing shareholders in proportion to the capital paid-up on shares held.
(iii) in case offered to any persons whether or not those persons include existing shareholders in any manner whatsoever:
   (a) special resolution was passed; or
   (b) else the votes cast in favour of the resolution exceeded the votes cast against the proposal, the approval of the Central Government was obtained;
   (c) in case of special resolution, e-Form 23 was filed with the Registrar.
(iv) the Board has approved the draft Letter of Offer of rights before issue;
(v) the company has complied with the SEBI (Disclosure and Investor Protection) Guidelines for issue of Rights Shares;
(vi) the appointments of all the agencies dealing with the issue were duly approved by the Board;
(vii) initial listing application(s) has/have been filed with the Stock Exchanges before mailing letter of offer;
(viii) the basis of allotment has been approved by the Regional Stock Exchange;
(ix) refund orders were sent in time;
(x) permission for listing has been obtained;
(xii) permission of the RBI has been obtained for export of the certificate.

Note: These provisions are not applicable to a director appointed by Central Government and a director holding office for life on 1.4.1952

(e) Approvals from the Shareholders

(a) If not less than 25 per cent of the subscribed capital of the company is held whether singly or in any combination by public finance institutions, etc. as mentioned in Section 224A, check whether the appointment of the auditor was approved by the members by passing a special resolution.

(b) Check whether the consent of the company in general meeting was obtained in respect of the matters specified under Section 293.

(c) If the company's paid-up share capital is Rs. 50 lakhs or more, check whether the appointment of sole selling agent was made with the consent of

the company accorded by special resolution and the approval of the Central Government (Section 294).

(d) Check whether appointment of sole-selling agent for any area was approved by the company in the first general meeting held after such appointment under Section 294.

(e) Check whether the approval under Section 314 by a special resolution was obtained consenting to the holding of any office or place of profit in the company by any director or other persons specified under Section 314.

(f) Check whether necessary resolutions were passed for the making of company loans and inter company investments under Section 372A of the Act.

(f) Approvals of Financial Institutions

Examine covenants contained in the loan agreements thoroughly and check whether:

(i) all notices required to be sent to the financial institutions have been duly sent; and

(ii) necessary approvals were obtained from the financial institutions wherever required.

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<th>LESSON ROUND-UP</th>
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<tr>
<td>Every company having a paid-up share capital of rupees ten lakh or more but less than rupees two crores is required to file with the Registrar of Companies (ROC), a Compliance Certificate obtained from a secretary in whole-time practice and also attach a copy of the certificate with a report of the Board of Directors of the Company.</td>
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<td>Compliance Certificate not only acts as an effective mechanism to ensure that the legal and procedural requirements under the Companies Act are duly complied with but also instills professional discipline in the working of the company besides building up the necessary confidence in the state of affairs of the company.</td>
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The scope of Compliance Certificate would comprise of certification of the compliance of various requirements under the Companies Act and the Rules thereunder.

The Practising Company Secretary should certify compliance only in respect of matters specified in the Form prescribed under the Rules and where any matter is not applicable, he should specify accordingly.

Practising Company Secretary for the purpose of issue of Compliance Certificate shall have right to access at all times to the registers, books, papers, documents and records of the company whether kept in pursuance of the Act or any other Act or otherwise and whether kept at the registered office of the company or elsewhere and shall be entitled to require from the officers or agents of the company, such information and explanations as the Practising Company Secretary may think necessary for the purpose of such certificate.

Where a company fails to comply with the requirement of filing the Compliance Certificate with the Registrar of Companies or attaching the copy of such certificate with Board’s report, in terms of Sub-section (1A) of Section 383A the company and every officer of the company who is in default shall be punishable with fine which may extend to Rs. 500 for every day during which the default continues.

SELF-TEST QUESTIONS

(These questions are meant for recapitulation only. Answers to these are not to be submitted for evaluation).

1. Discuss the scope and need of obtaining Compliance Certificate.
3. State the Checklist for (i) General Meetings; (ii) Meetings of Directors; (iii) Status of the company.
4. Discuss professional responsibility in the context of Compliance Certificate and the penal provisions for false statements.
5. Who can issue a Compliance Certificate? Are there any disqualifications prescribed.
STUDY XVI
SEARCH/STATUS REPORTS

LEARNING OBJECTIVES
The objective of this study lesson is to enable the students to understand
Legal provisions relating to charges.
e-filing of Form 8, 10, 17 etc.
Requirement of Financial Institutions and corporate lenders
Check-list for scrutiny of documents for preparing search report.

I. INTRODUCTION

Company as a separate entity has a facility of raising capital for earning large-scale profits, which is normally not within the purview of individual efforts and means. In the past, the companies used to raise money by way of issue of equity or preference shares. However, with the increasing pressure of capital requirements, different and alternative modes of financing were explored and the concept of loan capital came into being. The loan requirements of a company to be met, had to be raised frequently and also by a number of individuals as in the case of share capital. This brought to the fore the concept of pari passu ranking.

A charge is created when the security on the property of the company is conferred on another person. Where in a transaction for value, both parties evidence an intention that the property existing or future, shall be made available as security, the charge on the property is created.

The Companies Act, 1956 provides for a comprehensive list of charges which require registration and it also provides for the consequences of non-registration. The Act envisages registration of charges with the Registrar of Companies so that any person acquiring the property of the company has constructive notice of the charge prior to acquisition. Once a certificate of charge is issued by the Registrar of Companies, it is conclusive evidence that the document creating the charge is properly registered.

II. SEARCH/STATUS REPORTS

Banks and various State Financial/Industrial Investment Corporations, while granting loans to companies invariably obtain a status report on the position of borrowings made by the company and the particulars of charges already created by the company on its assets. This is a part of the security aspect of the amount proposed to be lent.

The Report, inter alia, informs the lenders, about the status of charges held by them vis-à-vis charges, if any held by others. The Search and Status Report acts as a tool to confirm and evidence information and contains information on status of charges. It is basically a report furnished based on the information gathered by a search of specific records made available for inspection in a Public Office or in any other convenient form. It is not merely verbatim reporting of the information as made available but also supplemented by observations/comments by the person who
furnishes the Report.

The Search and Status Report enables furnishing of information to the lender as to whether the charges created through various documents are in fact registered with Registrar of Companies and whether such particulars reflect the correct position of charges held by Lenders. As the Report provides information on the charges created in favour of other lenders, it enables the lenders to assess the exact position of the company and to foresee where they would stand, if the company would go into liquidation. Normally, practicing Company Secretaries are entrusted with the preparation of status/search reports.

Indian Banks' Association had issued a circular letter, recommending to the Chief Executives of all member banks that the latter may utilise the services of company secretaries for compilation of search/status reports and certification thereof.

III. SCOPE AND IMPORTANCE

The scope of a Search report depends upon the requirements of the Bank or Financial Institution concerned.

A Search report prepared by the Company Secretary in Practice enables the Bank/Financial Institution to evaluate the extent upto which the company has already borrowed moneys and created charges on the security of its movable and/or immovable properties. This information is very vital for considering the company's request for grant of loans and other credit facilities. The Bank/Financial Institution, while assessing the company's needs for funds, can take a conscious decision regarding the quantum of loan/credit facility to be sanctioned, sufficiency of security required and its nature, as also other terms and conditions to be stipulated. The Search report, thus, acts as an important source of information enabling the lending Bank/Institution to take an informed and speedy decision, and also assures it about the credit-worthiness or otherwise of the borrowing company.

IV. SEARCH/STATUS REPORT

A Search and Status Report as is apparent from its name contains two aspects. The first being 'search' which involves physical inspection of documents and the second activity 'status' which comprises of reporting of the information as made available by the search.

Thus a search and status report de facto acts as a ‘Progress Report’ on the legal aspects and also a ready reckoner of the exact position.

(a) Particulars of Charges

When a charge on the assets of the Company is created or modified or when a property subject to charge is acquired by a company, particulars thereof are filed in Form No. 8 with the Registrar of Companies (ROC). When the charge is satisfied, the fact is intimated in Form No. 17 to the ROC (now e-forms 8 and 17).

Particulars of a series of debentures containing or giving reference to any other instrument any charge to the benefit of which the debentureholders of the said series are entitled, are filed with the ROC in Form No. 10 (now e-form 10).

After the Registrar registers it, a certificate of registration of the charge is then
given by the ROC stating the amounts thereby secured. Such certificate is the conclusive evidence that the legal requirements relating thereto have been complied with.

(b) Examination of documents and registration

Prior to the launch of MCA-21, documents filed in the office of the ROC from time to time were taken-up for examination according to the date of filing.

When they were examined in the ROC's office, the documents if found complete and in order in all respects, were registered. Particulars of the registered documents were first entered in a loose-leaf register, an internal record in Registrar's office. Thereafter, they were sent to the Registry Section in Registrar's office for filing.

Only those documents which passed through all the aforesaid stages and had been duly filed in respective Document File of the Company at ROC were made available for inspection. Normally there was a time-lag between the date of filing and the date of availability of the documents for public inspection.

However, with the implementation of e-filing, this time lag will not be material.

MCA-21 offers the facility to view documents and also search and other facilities of public documents. This facility is handy for users and banks and financial institutions while sanctioning loans.

This facility enables viewing of public documents of companies for which payment has been made by user. The document can be viewed only within 7 days after the payment has been confirmed. Also, the documents are available for only 3 hours after the user has started viewing the first document of the company.

(a) User has to access My MCA portal and login to the My MCA portal.

(b) Click on the 'My Documents' tab after logging into the system.

(c) List of company names will be displayed, for which user have already paid for public viewing. It also displays

(i) Date of request i.e. the date, when user made the request to view the company document.

(ii) Status of the request i.e. whether viewed or to view.

(d) Click on the view link under status field.

(e) The documents are grouped under five categories i.e. user has to click on the desired category under which the document falls.

(f) If more than one document is listed, the user can arrange them name wise or date wise.

(g) On clicking the document name, the document shall be displayed for viewing.

The public documents under this facility are available for viewing by public on payment of requisite fee. Public documents include Incorporation documents, charge
documents, annual returns and balance sheet, change in directors and other
documents.

The Ministry, at present, is in the process of scanning and digitizing the records
of all active companies. It has vide O.M. No.HQ/73/2006-Computerisation dated
20.04.2006 issued a message to the public to view and verify Company Master Data
and Index of Charges, Apply for DIN, Procure Digital Signature Certificates (DSCs),
Procure DSCs for Banks/Financial Institutions, bring soft copy of the e-form and opt
to pay statutory fees through on line system.

The basic record on the basis of which the report was previously submitted to the
banks/institutions, was the Register of Charges maintained in the Office of the ROC.
With respect to each company, a Register of charges is maintained by the ROC. Prior
to 17.4.1989 the Register was kept in Form No. 13 prescribed under the Companies

Particulars of charges which are registrable with the ROC can be filed by the
company or the creditor (Section 125). Particulars of modification of charges have to
be filed only by the company concerned (Section 135). The satisfaction of any charge
in full has to be informed only by the company concerned under Section 138 except
in cases covered under Section 139. Thereafter, the Registrar would make
appropriate noting in the Register of Charges in accordance with Sub-section (2) of
Section 138.

(c) Inspection

Form 8, Form 10, Form 17 and copies of certificates of registration thereof are
available for inspection at the website.

Prior to introduction of e-filing the documents in the Document File at the ROC’s
office could be inspected by any person after making an application in writing and
paying Rs. 50* towards the fee. Normally, more than two persons were not allowed
to carry out jointly the inspection of Document File(s) of one company.

For knowing the volume number(s) and page number(s) in which the particulars
are entered in the Register(s) of Charges by the Registrar prior to 17th April, 1989, it
was necessary to examine in the Document File, respective Form 8 or Form 17 on
which the number of the relevant volume/page were written.

While taking the inspection at Registrar’s office, a verbatim copy of the contents
was not allowed. Notes could be made by using pencil. Pen or ballpen could not be
used for taking down the notes.

(d) Verification of Documents Relating to Charges

Before proceeding with the inspection it would be advisable for the company
secretary in practice to know if the concerned bank/financial institution or the client
requires the Search Report, in any specific format and if so, the contents of the
format.

Meticulous care will have to be taken in noting down the following particulars
from the Register of Charges:

(a) Date of registration (preferably with the serial number) of the document
(b) Date and nature of the document creating the charge
(c) Amount of the charge
(d) Brief particulars of the property charged
(e) Name and address of the person in whose favour the charge is created.

In respect of each of the charges created, it would be essential to identify the modifications effected from time to time by noting down carefully the following particulars:

(a) Date of registration of the document (preferably with the serial number)
(b) Nature and date of the instrument modifying the charge
(c) Effect of Modification.

Each modification should be noted in chronological order and the above particulars should be compiled together for each charge.

If and when the charge is satisfied, fool-proof identification of the exact charge which is satisfied is of paramount necessity. The following particulars can be noted chronologically by way of modification by the Search Report.

(a) Date of registration (preferably with the serial number) of the document
(b) Date of satisfaction.

Non-essential particulars of charges comprise of the gist of terms and conditions with regard to (a) mode of repayment (b) rate of interest and (c) margin; these need not be given in the Search Report unless specifically so required by the client.

If the client requires particulars of the charges pending registration, it is advisable to give a separate report based on the verification of the registers and records maintained by or available with the company.

Some financial institutions require a Report by Company Secretaries in Practice, on certain additional points relevant and important for them. A separate Report can be given after inspecting or verifying the documents and records available with the Registrar and/or the company. The points normally covered under such Report are:

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<th>Item</th>
<th>Records to be verified</th>
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<tr>
<td>(a)</td>
<td>Name of the Company</td>
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<tr>
<td></td>
<td>Memorandum of Association Certificate of Incorporation or Fresh Certificate of Incorporation/Change of Name.</td>
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</table>

(Note: If capital is raised other than by cash, it should be shown separately).

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<th>2</th>
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<tr>
<td>(b) Date of Incorporation</td>
<td>Certificate of Incorporation.</td>
</tr>
</tbody>
</table>
(c) Company Number/Corporate Identity Number | Certificate of Incorporation/Fresh Certificate upon change of name/Certificate of registration of CLB Order for shifting registered office to another State.

(d) Address of Registered Office | Form 18, Form 23 Resolution(s) of Board/General Body, Form 21 with copy of CLB Order.

(e) Name and address of present directors (with their date of joining) | Articles of Association, Form(s) 32, Register of Directors.

(f) Authorised Share Capital of the company divided into__________ Shares of Rs.___________ each | Memorandum of Association, Form 5, Form 23

(g) Paid-up Capital of the company divided into____________ Shares of Rs.______ each | Form 23, Form 2, Register of Members, Accounts Ledger

(h) List of Members with details as to shares held by each of them. The names of directors to be specifically mentioned in such list of share-holders (List of members holding shares of a specified monetary threshold is also asked for in some cases). | Form 2, Annual Return, Register of Members, Register of Directors.

(i) Provision in the Articles of Association as to affixation of common seal of the company. (Particulars as to the persons in whose presence the seal of the company can be affixed to any deed). | Articles of Association. If there is no specific cause and the Articles have adopted Table A, Regulation 84 of Table A may be referred.

(j) Main Objects of the company. | Information regarding the relevant objects in clause IIIA or IIIC in the Memorandum of Association.

(k) Whether the Memorandum of Association of the company contains provisions for borrowing and charging fixed and movable assets of the company for securing repayment of such secured borrowing. | In Memorandum of Association, careful examination of incidental objects in clause IIIB.

(l) Whether the Articles of the company contains provisions for nomination by the corporation a director on the board of the company. | Articles of Association of the company.

Apart from the above, the master data available at the My MCA portal can be resorted to.
Mere reproduction of the particulars of charges in form of Search and Status Report is not sufficient. It also requires:

— A thorough study of the particulars relating to the amount secured by the charge and the terms and conditions governing the charge.

— An analysis of the security available to a particular lender for its advances.

— A comparison of charges created in favour of a particular lender vis-à-vis other lenders.

In other words, it does not necessary mean verbatim reporting of the information as made available but also supplemented by observations/comments by the person who furnishes the Report.

In nutshell, the following have to be borne in mind:

— The Search and Status Report should give exact details of particulars of charges/modifications/satisfactions as effected, filed and registered from time to time.

— Identify those charges and modification of charges, which have been created in favour of a particular lender.

— Take the particulars of the documents creating the charge as specified in Form Nos.8 and 10.

— Ascertain as to whether the amount secured by the charge as per the documents executed has been duly mentioned.

— Ascertain as to whether ‘properties’ offered as security are mentioned as per the documents creating the charge and attached with the Forms and verify whether they are as per the terms of Sanction.

— Check whether the terms and conditions governing the charge have been mentioned.

— Ascertain whether the name of the lender is properly mentioned.

— In case of modification of charge ascertain whether the names of documents effecting the modification are mentioned and whether the particulars of modification are clearly mentioned.

— In case of charge, the particulars of documents attached with forms, amount secured by the charge as per the documents and/or sanction ticket, the properties/assets secured by the charge, the terms and conditions governing the charge and the name of the lender is properly mentioned in the relevant columns of Forms Nos.8.

Further, a Search and Status Report should always be supported by expert observations on the charges created by the borrower in respect of the subject lender. It is necessary to peruse the observations/comments offered and the same should be read in conjunction with the Report. The observations/comments of the experts/professional (company secretary in practice) will certainly help to throw additional light on certain points which would have missed the attention of the “lenders” when the Form Nos. 8 was presented before them for signature.

Company Secretary in Practice giving the above information is required to certify
that his report has been submitted on the basis of the search carried by him on a particular date, with the Registrar's office/MCA portal. He is also required to certify that the company has filed all returns/forms within stipulated time with the Registrar's office up to the date required to be filed in regard to the above matters and also to report, if any notices have been served upon the company for breaches/non-compliance of any provisions of the Companies Act, 1956.

(e) Compilation and Preparation of Search Report

Search Report compiled on the basis of the scrutiny of the above documents is, therefore, related and restricted to only those documents which are available for the inspection on the date(s) when the search is carried out.

An index of the charges is prepared at the website of MCA. This index provides, charge ID, the date of filing of the document charge amount secured, name of chargeholder and its address. In order to view index of charges, it is primarily necessary to quote CIN/FCRN of the company. This number will primarily be available at the website of the ministry.

It is advisable to note down from the index, the short particulars of all Form Nos. 8, 10, and 17 for the purpose of cross-checking and ensuring that no document is missed in the Search Report.

Also, it would be advisable to mention in the Search Report by way of a footnote as to what was the last document which was available for inspection when the scrutiny was taken/completed. This information can be helpful in identifying the forms and based on which the Search Report is given. If a charge which is registered and in respect of which the certificate of registration is issued by the Registrar, but, if the document is not available for inspection, the aforesaid footnote can readily clarify the position.

(f) Format of Search Report and its Preparation

Some of the banks and financial institutions insist that the Search Report be given in their own format. It would, therefore, be advisable to know if any specific format is insisted upon by the client.

In the absence of any specific format, the Search Report may be given in the format given at Annexure 1.

A specimen copy of the format of Search Report as prescribed by Gujarat State Financial Corporation is given at Annexure 2.

V. LEGAL PROVISIONS

Sections 124 to 145 in Part V of the Companies Act, 1956 provide for the registration of charges in so far as any security on the company's property or undertaking is conferred, modified or satisfied thereby.

Prescribed particulars of the charge together with the instrument, if any, evidencing, creating or modifying the charge (or a certified copy thereof) are required to be filed with the Registrar of Companies within thirty days after the date of creation or modification of the charges. In case of satisfaction of charge, the intimation is
required to be given to the Registrar within thirty days from the date of payment or satisfaction of the charge.

The Registrar has discretionary powers to condone the delays upto thirty days in case of particulars relating to creation or modification of the charge. In the case of satisfaction of charge, the delays can be condoned by Company Law Board Bench of the respective regions upon a petition (application) filed by the company or interested person.

The prescribed particulars in Form 8 or Form 10 together with copy of the instrument creating or modifying the charge and those relating to satisfaction of charge in Form 17 are required to be filed with the Registrar of Companies. All these forms should be in triplicate and should be duly signed on behalf of the concerned company as well as the respective charge holder.

Non-filing of particulars of a charge renders the charge void against the liquidator or against any other creditor of the company. This implies that if particulars of a subsequent charge created on the property are filed and the particulars of the earlier charge particulars are not filed, then the subsequent charge-holder would enjoy precedence over the earlier charge-holder, e.g., in selling the property in order to satisfy his debt. It should be noted that the concerned company cannot, even in the event of non-filing of particulars of charge, repudiate its contractual obligation vis-à-vis the creditor in whose favour charge is created.

The following tables depicts the manner of verifying forms 8/10/17 relating to charges:

**TABLE A**

<table>
<thead>
<tr>
<th>Sl. No.</th>
<th>Relevant Provisions</th>
<th>Charges under Reference</th>
<th>Illustrative Instruments</th>
<th>To Verify Whether Or Not</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1)</td>
<td>(2)</td>
<td>(3)</td>
<td>(4)</td>
<td>(5)</td>
</tr>
<tr>
<td>I.</td>
<td>Sub-section (4) of Section 125 of the Companies Act, 1956</td>
<td>(a) a charge for the purpose of securing any issue of debentures</td>
<td>(a) Hypothecation or mortgage including floating charge</td>
<td>*The instrument is executed and is dated</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(b) a charge on uncalled share capital of the company</td>
<td>(b) Deed of assignment</td>
<td>*The common seal is affixed and if yes, the authority thereof is mentioned</td>
</tr>
<tr>
<td>(1)</td>
<td>(2)</td>
<td>(3)</td>
<td>(4)</td>
<td>(5)</td>
</tr>
<tr>
<td></td>
<td>(c) a charge on any immovable</td>
<td>(c) Mortgage</td>
<td></td>
<td>*The instrument bears adequate</td>
</tr>
</tbody>
</table>

TABLE A

Charges Requiring Registration
<table>
<thead>
<tr>
<th>(1)</th>
<th>(2)</th>
<th>(3)</th>
<th>(4)</th>
<th>(5)</th>
</tr>
</thead>
<tbody>
<tr>
<td>property, wherever situate, or any interest therein</td>
<td>stamps in accordance with the applicable Stamp Act</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(d) a charge on any book debts of the company</td>
<td>(d) Hypothecation *The instrument creates the charge specifying the amount of charge and the assets charged</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(e) a charge, not being a pledge, on any movable property of the company</td>
<td>(e) Hypothecation *The instrument modifying a charge refers to the original charge under modification and spells the extent of modification</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(f) a floating charge on the undertaking or any property of the company including stock-in-trade</td>
<td>(f) Hypothecation *The instrument bears names of the persons in whose favour the charge is created or modified</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(g) a charge on calls made but not paid</td>
<td>(g) Deed of assignment *The instrument contains the terms relating to (a) mode of repayment, (b) applicable rate/s of interest, (c) margin and (d) priority or precedence of charge/s</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(h) a charge on a ship or any share in ship</td>
<td>(h) Hypothecation</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(i) a charge on goodwill, or on a patent or a license</td>
<td>(i) Deed of assignment</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Event</td>
<td>Time Limit</td>
<td>Effect</td>
<td>Relevant provisions</td>
<td></td>
</tr>
<tr>
<td>-------</td>
<td>------------</td>
<td>--------</td>
<td>---------------------</td>
<td></td>
</tr>
<tr>
<td>Creation of charge or modification of charge or acquisition of property which is subject to charge</td>
<td>Within thirty days after the date of creation, modification or acquisition</td>
<td>The date when the event takes place is to be excluded while calculating the limit</td>
<td>Sections 125, 127 and 135 of the Act.</td>
<td></td>
</tr>
<tr>
<td>Satisfaction of the charge.</td>
<td>Within thirty days from the date of satisfaction</td>
<td>The date when the event takes place is to be excluded while calculating thirty days</td>
<td>Section 138 of the Act</td>
<td></td>
</tr>
<tr>
<td>The last day when the Form is to be delivered for registration with the Registrar</td>
<td>Within thirty days after the date of creation/modification/acquisition or from the date of satisfaction</td>
<td>On the last day when the Form has to be filed if on that day, the Registrar's Office is closed, the Form can be filed on the next day onwards on which the office is open</td>
<td>Section 10 of the General Clauses Act, 1897</td>
<td></td>
</tr>
</tbody>
</table>

VI. REQUIREMENTS OF VARIOUS FINANCIAL INSTITUTIONS AND OTHER CORPORATE LENDERS

The All-India Financial Institutions while granting term loans to companies insist on certain formalities to be completed by a company availing such loan. These
include furnishing of certificates by Company Secretaries in Practice in regard to the following:

(a) Necessary power of a company and its directors to enter into an agreement.

(b) Borrowing limits of a company under Section 293(1)(d) of the Companies Act, 1956, including details of share capital – authorised, issued, subscribed and paid-up, and the actual borrowing.

(c) List of members of a company.

(d) Copies of resolutions passed at company meeting to be furnished to financial institutions.

Many State Financial/Industrial Investment/Development Corporations have also agreed to accept the certificates issued by Company Secretaries in Practice, in regard to all/some of the aforesaid matters.

Certification by Company Secretaries in Practice

The certification to be done by Company Secretaries in Practice has to conform to any specific requirement of the Institution/Corporation. It may be stated that the matters to which certification extends can be verified by the Institutions themselves from the Memorandum/Articles of Association of companies, which are submitted to them. However, Institutions, by way of abundant caution insist for stipulation on certificates by independent professionals like Company Secretaries in Practice, in respect of these matters. The various certifications are explained in the following paragraphs.

Necessary Powers of a Company and its Directors to Enter into an Agreement

The Memorandum and Articles of Association of the company has to be examined for this purpose. Particularly the objects clause of the Memorandum of Association has a specified recital pertaining to borrowing powers of the company. The standard clause pertaining to borrowing powers included in the incidental or ancillary objects reads as follows:

“To borrow or raise money or to receive money on deposit for the purposes of the company, in such manner and upon such terms as may seem expedient, and to secure the repayment thereof and of moneys owing or obligations incurred by the company, and to create, issue and allot redeemable or irredeemable bonds, mortgages or other instruments, mortgage debentures (such bonds or debentures being made payable to bearer or otherwise and issuable or payable either at par, premium, discount, or as fully paid), and for any such purposes to charge all or any part of the property and profits of the company both present and future including its uncalled capital”.

A trading or commercial company has implied power to borrow even though there is no express authority in its Memorandum of Association.

Compliance of the provisions of Section 149 of the Companies Act, 1956, in respect of public limited companies has to be ensured. Exercise of borrowing powers in contravention of Section 149 attracts levy of fine.

Resolutions passed at the meeting of the board/general meeting for exercising
the power of borrowing have to be checked; in the absence of any provision to the contrary in the articles of association, the borrowing power may be exercised by the Board of directors.

Section 292 of the Companies Act requires *inter alia*, that the power to borrow moneys otherwise than on debentures can be exercised by the Board of Directors only by means of resolution passed at meetings of the Board. This power of borrowings may also be delegated to any committee of directors, managing director, manager or any other principal officer. The delegation should be only by means of resolution passed at board meeting and not by circulation. Every resolution delegating this power should specify the total amount upto which moneys may be borrowed by the delegate.

The financial institutions require that this certificate will have to refer to the relevant clause(s) of the Memorandum of Association of the company, which gives specific powers to the company, and to secure the repayment of the same by mortgage, charge, lien, etc. the opinion will also have to refer to the relevant article(s) of the Article of Association and the general body resolution, if any, under which the Board of Directors are authorised to borrow or raise moneys, secure the repayment thereof and execute on behalf of the company, bonds, deeds, documents, etc. The opinion should also spell out the limitations and restrictions, if any, on the powers of the Board of directors to borrow or raise money.

**Borrowing Limits and Compliance of Section 293(1)(d)**

(i) In the case of a public company or a private company which is a subsidiary of a public company, the consent of general meeting is required if the moneys to be borrowed alongwith the moneys already borrowed exceeds the aggregate of paid-up capital and free reserves. If the borrowings exceed this limit check the minutes of the general meeting of members to ensure that the Board is authorised to borrow and also that the proposed borrowing does not exceed the amount specified in the resolution passed by the company in general meeting. Temporary loans repayable on demand or within six months obtained from the company’s bankers in the ordinary course of business are excluded from the purview of borrowings under this section.

(ii) Obtain a certified true copy of the resolution passed by the members of the company under Section 293(1)(d) of the Companies Act, 1956.

(iii) Check the resolution passed by the Board to borrow the money.

(iv) Check the latest audited balance sheet of the company for verifying the amount of share capital, free reserves and the total amount of borrowings.

(v) Also check the Register of Charges.

‘Free reserve’ means, “reserves not set apart for any specific purpose”.

Any change in these items after the date of balance sheet should be checked from the accounts of the company, allotment register and agreements entered to borrow the moneys and such other records and documents.

**List of Members of the Company**
The requirements of the financial institutions vary on a case to case basis in regard to list of members of the company to be furnished. The certificate by a Company Secretary in Practice has therefore to meet with any specific stipulation by the Institution(s). The Certificate has to be based on an examination of the Register of Members maintained by the Company under Section 150 of the Companies Act, 1956.

Copies of Resolutions Passed at Company Meetings to be Furnished to Financial Institutions

A Company Secretary in Practice has been recognised to certify resolutions passed at company meetings. Which IFCI copies of the following resolutions can be certified by a Company Secretary in Practice:

(i) Resolution to be passed by the company in general meeting in pursuance of Section 293(1)(d) of the Companies Act, 1956.

(ii) Ordinary resolutions to be passed by the company at the general meeting under Section 293(1)(a) of the Companies Act, 1956.

(iii) Resolutions to be passed at a meeting of the Board of Directors of the borrower for acceptance of the terms and conditions of letter of intent and execution of documents.

Certificate of Adequacy of Insurance to be Submitted Every Half Year

The IFCI has recognised certificate from a Company Secretary in Practice in regard to adequacy of insurance to be submitted every half year viz. on 30th June and 31st December. Before giving the certificate it is necessary to verify the original insurance policies and check carefully the details of properties covered by the policy. Particular attention shall be paid to ‘Statement of Insurance Cover’ and if that clause is applicable, the certificate should clearly give an explanatory statement.

ANNEXURES

ANNEXURE 1

Format of Search Report

Search report
On
the charges on the assets of
................................. Limited
(Company Number..............)

I/We have carried out the search of the Register of Charges and the documents related to the charges on the assets of the above named Company as registered by and available for inspection on............................ at the office of Registrar of Companies*.............. and hereby report that the following particulars of charges in respect of the above-named Company have been so registered:

<table>
<thead>
<tr>
<th>Sl.</th>
<th>Date of Instrument creating</th>
<th>Amount of</th>
<th>Short Particulars of</th>
</tr>
</thead>
</table>

* Now available on the website.
<table>
<thead>
<tr>
<th>No.</th>
<th>registration</th>
<th>charge and date</th>
<th>charge Rs.</th>
<th>property charged</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1)</td>
<td>(2)</td>
<td>(3)</td>
<td>(4)</td>
<td>(5)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Name &amp; address of Person in whose favour the charge is created</th>
<th>Particulars of Modification</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Date of registration</td>
</tr>
<tr>
<td></td>
<td>(6)</td>
</tr>
</tbody>
</table>

Notes:
1. The figures in bracket in column numbers 2 and 7 indicate the serial numbers under which the respective documents have been registered.
2. The last document registered in the Document File and available for inspection at the office of Registrar of Companies, …………………
3. ………………………
4. ………………………

(Signature with seal)
Name and Address of Company Secretary in Practice……………

Place: ……………………… Certificate of Practice No. …………………
Date: ……………………… Membership No. ……………………………

ANNEXURE 2

CONTENTS OF SEARCH REPORT AS FORMATTED BY GUJARAT STATE FINANCIAL CORPORATION (GSFC)

Gujarat State Financial Corporation, a Government of Gujarat undertaking formed under the State Financial Corporation Act, 1951 (GSFC) has recognised the utility of services of Company Secretaries in Practice since October, 1982 and has been availing their certifications in several areas.

For Search reports and other work connected with the office of the Registrar of Companies, recently GSFC has carved out exclusive area for Company Secretaries in Practice.

Unlike Search Report based on the Inspection of Document File of the company available with the Registrar of Companies (ROC), the Search Report for GSFC is
based on the scrutiny of Document File at ROC as well as the registers/records maintained and the information provided to the professional by the Company. The object behind the Search Report is to know up-to-date and authentic information relating to the company certified by an independent professional.

An attempt is made hereinafter to examine the contents of Search Report as presently formatted by GSFC.

To be given on the letterhead of Company Secretary in Practice

GUJARAT STATE FINANCIAL CORPORATION

SEARCH REPORT

Date:

The Dy. Gen. Manager (Legal)
GSFC
Ahmedabad

Dear Sir,

Re.: M/s______________________________________________________
Dist.:___________ Financial Assistance from Gujarat State Financial Corpn.

At the instance of Shri____________________________, Director of the aforesaid company, we have carried out searches of the Register of Charges and records as maintained by the Office of the Registrar of Companies on_________________________ on_________________________ and also on verification of the records maintained by the company and the information/papers provided/furnished by the company in this behalf, we have to report as under:

<table>
<thead>
<tr>
<th>Sl. No.</th>
<th>Matter under GSFC Format</th>
<th>Documents to be checked</th>
<th>Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1)</td>
<td>(2)</td>
<td>(3)</td>
<td>(4)</td>
</tr>
<tr>
<td>1.</td>
<td>Name of Company</td>
<td>(i) Name-Clause in Memorandum of Association (ii) Certificate of Incorporation</td>
<td>If name is changed also to check 1. Copy of Special Resolution 2. Form No. 23 3. Revised Certificate of Incorporation.</td>
</tr>
<tr>
<td>2.</td>
<td>Date of its incorporation and Company No. Address of Registered</td>
<td>Certificate of Incorporation, Board Resolution and Copy of</td>
<td>If shifted outside local limits, also to check Special Resolution &amp;</td>
</tr>
</tbody>
</table>

* Inspection can now be done online also.
<table>
<thead>
<tr>
<th><strong>Office</strong></th>
<th><strong>Form No. 18</strong></th>
<th><strong>Form No. 23.</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>If shifted to another State also to check: (a) Special Resolution, (b) Form 23 (c), CLB Order &amp; Form 21 &amp; its registration by ROC.</td>
</tr>
</tbody>
</table>

3. **Name & address of present directors**
   (1) Board/General Body Resolutions
   (2) Register of Directors
   (3) Form Nos. 32 & 29*  
   Communications about nominations, changes in particulars, if any, also to be checked.

4. **Whether the company is empowered by its Memorandum to undertake manufacturing activity of the nature for which project is being set up and financed by the Corporation**
   GSFC Consent Letter & Clause IIIA of Memorandum of Association/Clause IIIC of Memorandum of Association  
   — In case of public company, also to check Special Resolution, Form 23 and the Declaration. If objects are altered, also to check Special Resolution, Form 23 (Form 21 along with CLB Order, if any) and their registration.

5. **(i) Authorised Capital of the Company**
   Clause V of Memorandum of Association  
   If altered, Special/Ordinary Resolutions and Form Nos. 5/23

   **(ii) Paid-up Capital of the Company**
   Note: If capital is raised otherwise than by cash, it should be shown separately.
   (i) Book of Accounts
   (ii) Form No. 2

   **(iii) List of members with details as to shares held by each of them. The names of directors, by specifically mentioning in such list of share-**
   Register of Members
   Whether a member is a director or not should be separately mentioned after verifying Register of Directors.

* No more relevant.
<p>| | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>(iv) Percentage of directors holding in the paid-up capital of the company.</td>
<td>Register of Members Register of Directors Books of Accounts</td>
<td>—</td>
</tr>
<tr>
<td>6. Particulars of Charges, if any created by the Company (As per the Annexure) pending for registration.</td>
<td>Register of Charges under Sections 130 and 143</td>
<td>(1) GSFC requires separately the particulars of charges (a) as registered by ROC (b) as well as pending registration. (2) Particulars of charge pending registration can be compiled from the Register of Charges maintained by the company and should invariably be supported by the proof of filing of the relevant particulars with ROC i.e. Money Receipt.</td>
</tr>
<tr>
<td>7. Provision as to affixing of seal on the document/s in the Articles of Association of the Company.</td>
<td>Articles of Association</td>
<td>If the company's Articles adopt Table A, Regulation 84 thereof.</td>
</tr>
<tr>
<td>8. Whether the company has filed all returns-forms- particulars within stipulated time as required under Companies Act/Rules with ROC in regard to above matters and whether any notice has been served on the company and/or its directors for breaches/non-compliance of any provisions of Companies Act/Rules.</td>
<td>(1) All Minutes of Meetings of Directors and Shareholders. (2) All Statutory Registers (3) Communications from Directors &amp; Shareholders. (4) Communications with ROC/RD/DCA.*</td>
<td>—</td>
</tr>
</tbody>
</table>

* However, the provision of Section 43A has been repealed by companies (Amendment) Act, 2000.
<p>| | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>9.</td>
<td>Whether there are provisions in the Memorandum of the company for long term borrowings and charging of immovable and movable assets wholly or partly of the industrial undertaking of the company in favour of lenders for securing repayment of such secured borrowings.</td>
<td>Clause IIIB of the Memorandum of Association</td>
</tr>
<tr>
<td>10.</td>
<td>Whether the Articles of Association of the company contain the provisions for nomination by the Corporation of the Director/s on the company.</td>
<td>Articles of Association</td>
</tr>
</tbody>
</table>
| 11. | Whether the company has become a deemed public company (state the reasons which attracted provision of Section 43A of the Companies Act).** | — Register of Members  
— Resolution/s of the Board/Shareholders  
— Register of Investments |  |
| 12. | Whether the company is statutorily required to appoint ‘Company Secretary’. If so, give the name of the Secretary appointed by the company. | — Books of Accounts  
— Form No. 2  
— Form No. 32  
— Board Resolution, if any. |  |

** MCA.
**LEARNING OBJECTIVES**

The search/status report enables furnishing of information to the under as to whether the charges created through various documents are in fact registered with ROC and whether such particulars reflect the correct position of charges held by lenders.

MCA21 offers the facility to view documents which is handy for banks and financial institutions while granting loans.

The scope of search report depends upon the requirements of the bank or financial institution concerned.

Search/status report prepared by PCS enables banks/financial institutions to evaluate the extent up to which the company has already borrowed moneys or created charges on scrutiny of its movable and/or immovable properties.

**SELF-TEST QUESTIONS**

*(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation.)*

1. What is a status/search report? Discuss the format normally followed for this report.

2. State the general points to be kept in mind by Company Secretary in Practice while preparing status/search report.

3. What are the certifications recognised by Financial Corporations/Institutions to be furnished to them by Company Secretary in Practice.

4. State the procedure of registering charges (created/modified) with the Registrar of Companies as required under Section 124 to 145 of the Companies Act 1956.
STUDY XVII
SECURITIES MANAGEMENT AND COMPLIANCES

LEARNING OBJECTIVES

The objective of this study lesson is to enable the students to understand
Meaning need and scope of securities management and compliances
Securities management as a mechanism for self-regulation
Advantages of securities management to company, regulator and investor

I. INTRODUCTION

Securities Management and Compliances is not a new concept in the Indian
securities market. It exists in different forms of certifications, verifications, etc.
However, in view of reforms in capital market, the increase in corporate population,
aberrations in capital market and investors’ grievances, Securities Management and
Compliances has become an imperative for ensuring good governance in capital
market and investor confidence.

SEBI was established with the twin objectives of protecting the interest of the
investors in securities and also regulating and promoting the development of the
securities markets. SEBI, in order to achieve its objectives, has formulated various
Rules and Regulations along with guidelines applicable to all the players of capital
market both primary and secondary market. However, inspite of existence of a
number of Rules, Regulations and Guidelines the markets remained vulnerable to the
non-compliances and shareholders grievances.

At present, the transactions in securities are governed, regulated and controlled
by Companies Act, 1956, Securities and Exchange Board of India Act, 1992,
Securities Contracts (Regulation) Act, 1956, Foreign Exchange Management Act,
1999, Depositories Act, 1996, Stamp Act, 1899, Information Technology Act, 2000,
Competition Act, 2002 including rules, regulations made and guidelines and
directions issued thereunder and bye-laws of stock exchanges and Listing
Agreement, etc. Inspite of plethora of statutes, Rules, Regulations and Guidelines,
there is no mechanism to ensure proper and comprehensive compliances,
monitoring and management of these statutory provisions in relation to securities.
In order to provide a mechanism to comprehensively ensure compliance of all
provisions relating to securities, to redress the grievances of investors, strengthen
the faith of investors in capital market, ensure the growth of capital market,
prevent the fraudulent and unfair trade practices, instill professional discipline
and to protect the interest of investors, it is necessary to introduce the mechanism
of “Securities Management and Compliances”.

II. SECURITIES — CONCEPT AND INTERPRETATION

The term ‘securities’ has been defined under Securities Contracts (Regulations)
Act, 1956; Companies Act, 1956; Securities and Exchange Board of India Act, 1992
and Foreign Exchange Management Act, 1999.
As per Section 2(1)(i) of the Securities and Exchange Board of India Act, 1992 ‘securities’ has the meaning assigned to it in Section 2 of the Securities Contracts (Regulation) Act, 1956.

As per Section 2(aa) of the Securities Contracts (Regulation) Act, 1956, Derivative includes –

(a) a security derived form a debt instrument, share, loan, whether secured or unsecured, risk instrument or contract for differences or any other form of security;

(b) a contract which derives its value from the prices or index of prices, of underlying securities.

A derivative is a product whose value is derived from the value of underlying asset, index, etc. The underlying assets can be equity, forex commodity, or any other asset.

As per Section 2(45AA) of the Companies Act, 1956 ‘securities’ means securities as defined in clause (h) of Section 2 of the Securities Contracts (Regulation) Act, 1956, and includes hybrids.

As seen from above the term ‘securities’ as defined in Companies Act, 1956 and Securities Exchange Board of India Act, 1992 is mainly dependent on the definition given in Securities Contract (Regulations) Act, 1956.

As per Section 2(h) of Securities Contract (Regulations) Act, 1956 securities include

(i) shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate;

(ia) derivative;

(ib) units or any other instruments issued by any collective investment scheme to the investors in such schemes;

(ic) security receipt as defined in clause (zg) of Section 2 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002

(ii) Government securities;

(iia) such other instruments as may be declared by the Central Government to be securities; and

(iii) rights or interests in securities;

Many terms have been used in order to define the term Securities. However, Securities Contracts (Regulation) Act, 1956 defines only the terms ‘derivatives’ and ‘government securities’ out of all terms used in defining the term ‘securities’.

As per Section 2(b) of Securities Contract (Regulation) Act, 1956 ‘Government security’ means a security created and issued, whether before or after the commencement of this Act, by the Central Government or a State Government for the purpose of raising a public loan and having one of the forms specified in clause (2) of
section 2 of the Public Debt Act, 1944.

As per Section 2(za) of the Foreign Exchange Management Act, 1999 ‘security’ means shares, stocks, bonds and debentures, government securities as defined in the Public Debt Act, 1944, savings certificates to which the Government Savings Certificates Act, 1959 applies, deposit receipts in respect of deposits of securities and units of the Unit Trust of India established under Sub-section (1) of Section 3 of the Unit Trust of India Act, 1963 or of any mutual fund and includes certificates of title to securities, but does not include bills of exchange or promissory notes other than government promissory notes or any other instruments which may be notified by the Reserve Bank as security for the purposes of the Act;

As per Section 2(12B) of the Companies Act, 1956 ‘derivative’ has the same meaning as in clause (aa) of Section 2 of the Securities Contracts (Regulations) Act, 1956.

As per Section 2(19A) of the Companies Act, 1956 ‘hybrid’ means any security which has the character of more than one type of security, including their derivatives.

Hybrid securities mean securities which have some of the attributes of both debt securities and equity securities. A type of security which, in the form of a debenture, contains elements of indebtedness and elements of equity stock also is an example of a hybrid.

The terms share and debenture used in the definition of securities have been defined in the Section 2(46) and 2(12) of Companies Act 1956, respectively. Share means share in the share capital of a company, and includes stock except where a distinction between stock and shares is expressed or implied. A share reflects the contribution of a shareholder towards the share capital of the company. As per Section 82 of the Companies Act, 1956 share is a movable property. A share is a right to a specified amount of the share capital of a company, carrying with it certain rights and liabilities, while the company is a going concern and in the winding-up it represents the interest of the holder measured for purposes of a liability and divided by a sum of money. A share is the interest of a shareholder in the company measured by a sum of money, for the purpose of liability in the first place and of the interest in the second, but also consisting of a series of mutual covenants entered into by all the shareholders inter se.

Debenture means a document which either creates or acknowledges a debt. It is also a method of raising loans. As per Section 2(12) of the Companies Act, 1956. Debenture includes debenture stock, bonds and any other securities of a company, whether constituting a charge on the assets of the company or not.

Debenture stock is of the same nature as debentures but instead of each lender having a separate debenture bond; he gets a certificate entitling him to a specified portion of one large loan. Debenture stock is consolidated borrowed capital which may be divided into and is transferable in convenient units of fixed amount.

Considering all the above-mentioned definitions it can be inferred that the term ‘security’ includes shares, debentures, government securities, derivatives, units and rights and interest in securities.

III. FUNCTIONS OF SECURITIES MARKET
The Securities Market allows people to do more with their savings than they would otherwise could. It also provides financing that enables people to do more with their ideas and talents than would otherwise be possible. The people's savings are matched with the best ideas and talents in the economy. Stated formally, the Securities Market provides a linkage between the savings and the investment across the entities, time and space. It mobilises savings and channelises them through securities into preferred enterprises.

The Securities Market also provides a market place for purchase and sale of securities and thereby ensures transferability of securities, which is the basis for the joint stock enterprise system. The existence of the Securities Market makes it possible to satisfy simultaneously the needs of the enterprises for capital and the need of investors for liquidity.

The liquidity the market confers and the yield promised or anticipated on security ownership may be sufficiently great to attract net savings of income which would otherwise have been consumed. Net savings may also occur because of other attractive features of security ownership, e.g. the possibility of capital gain or protection of savings against inflation.

A developed Securities Market enables all individuals, no matter how limited their means, to share the increased wealth provided by competitive private enterprises (Jenkins, 1991)\(^1\). The Securities Market allows individuals who can not carry an activity in its entirety within their resources to invest whatever is individually possible and preferred in that activity carried on by an enterprise. Conversely, individuals who can not begin an enterprise, they can attract enough investment from others to make a start. In both cases individuals who contribute to the investment made in the enterprise share the fruits.

The Securities Market, by allowing an individual to diversify risk among many ventures to offset gains and losses, increases the likelihood of long-term, overall success.

IV. SECURITIES MARKET AND ECONOMIC GROWTH

A well functioning securities market is conducive to sustained economic growth. There have been a number of studies, starting from World Bank and IMF to various scholars, which have established robust relationship not only one way, but also the both ways, between the development in the securities market and the economic growth. The securities market fosters economic growth to the extent that it—(a) augments the quantities of real savings and capital formation from any given level of national income, (b) increases net capital inflow from abroad, (c) raises the productivity of investment by improving allocation of investible funds, and (d) reduces the cost of capital.

It is reasonable to expect savings and capital accumulation and formation to respond favourably to developments in securities market. The provision of even

simple securities decouples individual acts of saving from those of investment over both time and space and thus allows savings to occur without the need for a concomitant act of investment. If economic units rely entirely on self-finance, investment is constrained in two ways: by the ability and willingness of any unit to save, and by its ability and willingness to invest. The unequal distribution of entrepreneurial talents and risk taking proclivities in any economy means that at one extreme there are some whose investment plans may be frustrated for want of enough savings, while at the other end, there are those who do not need to consume all their incomes but who are too inert to save or too cautious to invest the surplus productively. For the economy as a whole, productive investment may thus fall short of its potential level. In these circumstances, the securities market provides a bridge between ultimate savers and ultimate investors and creates the opportunity to put the savings of the cautious at the disposal of the enterprising, thus promising to raise the total level of investment and hence of growth. The indivisibility or lumpiness of many potentially profitable but large investments reinforces this argument. These are commonly beyond the financing capacity of any single economic unit but may be supported if the investor can gather and combine the savings of many. Moreover, the availability of yield bearing securities makes present consumption more expensive relative to future consumption and, therefore, people might be induced to consume less today. The composition of savings may also change with fewer saving being held in the form of idle money or unproductive durable assets, simply because more divisible and liquid assets are available.

**International Linkage**

The securities market facilitates the internationalisation of an economy by linking it with the rest of the world. This linkage assists through the inflow of capital in the form of portfolio investment. Moreover, a strong domestic stock market performance forms the basis for well performing domestic corporate to raise capital in the international market. This implies that the domestic economy is opened up to international competitive pressures, which help to raise efficiency. It is also very likely that existence of a domestic securities market will deter capital outflow by providing attractive investment opportunities within domestic economy.

**V. CONCEPT AND NEED OF SECURITIES MANAGEMENT AND COMPLIANCES**

The functions, operation and management of a company are governed by various Acts, Rules and Regulations. The Companies Act, 1956 is one of the major legislations dealing with various activities of a company, and it has to be complied with even before the company comes into existence. Every company needs funds for the smooth functioning of its business, to expand its business, diversify its business etc. The company has to issue various types of securities to meet its requirement of funds. The issuance of any kind of security is again subject to the compliances of various Acts, Rules, Regulations and Guidelines. Once the securities have come into existence, the transactions in the securities are also governed by various Acts, Rules and Regulations. Not only the issuer of the securities but also the holder of the securities are required to comply with the statutory provisions to transact in the securities of the company.

The concept of Securities Management and Compliances thus signifies and includes in its ambit examination, verification or checking of registers, records, forms, returns and documents relating to securities issued by a company and certification of
timely and proper compliance of all statutory provisions related to securities applicable to a company.

Thus Securities Management and Compliances, can provide an umbrella mechanism to ensure better compliances of all the statutory provisions relating to securities by the companies.

The Company Secretary of a company, shall ensure the management of securities issued by the company, timely compliance of relevant provisions of law applicable to the securities so issued and maintain all records and documents relating to securities issued by the company.

VI. SCOPE OF SECURITIES MANAGEMENT AND COMPLIANCES

The four main legislations governing the securities market are: (a) the SEBI Act, 1992 which establishes SEBI to protect investors and develop and regulate securities market; (b) the Companies Act, 1956, which sets out the code of conduct for the corporate sector in relation to issue, allotment and transfer of securities, and disclosures to be made in public issues; (c) the Securities Contracts (Regulation) Act, 1956, which provides for regulation of transactions in securities through control over stock exchanges; and (d) the Depositories Act, 1996 which provides for electronic maintenance and transfer of ownership of demat securities.

Legislations

SEBI Act, 1992: The SEBI Act, 1992 establishes SEBI with statutory powers for (a) protecting the interests of investors in securities, (b) promoting the development of the securities market, and (c) regulating the securities market. Its regulatory jurisdiction extends over corporates in the issuance of capital and transfer of securities, in addition to all intermediaries and persons associated with securities market. It can conduct enquiries, audits and inspection of all concerned and adjudicate offences under the Act. It has powers to register and regulate all market intermediaries and also to penalise them in case of violations of the provisions of the Act, Rules and Regulations made there under. SEBI has full autonomy and authority to regulate and develop an orderly securities market. The details have been covered ahead in the chapter.

Securities Contracts (Regulation) Act, 1956: It provides for direct and indirect control of virtually all aspects of securities trading and the running of stock exchanges and aims to prevent undesirable transactions in securities. It gives central government/SEBI regulatory jurisdiction over (a) stock exchanges through a process of recognition and continued supervision, (b) contracts in securities, and (c) listing of securities on stock exchanges. As a condition of recognition, a stock exchange complies with prescribed conditions of Central Government. Organised trading activity in securities takes place on a specified recognised stock exchange. The stock exchanges determine their own listing regulations which have to conform to the minimum listing criteria set out in the Rules. The details have been discussed in the Chapter on Stock Exchanges.

Depositories Act, 1996: The Depositories Act, 1996 provides for the establishment of depositories in securities with the objective of ensuring free transferability of securities with speed, accuracy and security by (a) making securities
of public limited companies freely transferable subject to certain exceptions; (b) dematerialising the securities in the depository mode; and (c) providing for maintenance of ownership records in a book entry form. In order to streamline the settlement process, the Act envisages transfer of ownership of securities electronically by book entry without making the securities move from person to person. The Act has made the securities of all public limited companies freely transferable, restricting the company’s right to use discretion in effecting the transfer of securities, and the transfer deed and other procedural requirements under the Companies Act have been dispensed with. The details have been dealt in the chapter on Depositories.

Companies Act, 1956: It deals with issue, allotment and transfer of securities and various aspects relating to company management. It provides for standard of disclosure in public issues of capital, particularly in the fields of company management and projects, information about other listed companies under the same management, and management perception of risk factors. It also regulates underwriting, the use of premium and discounts on issues, rights and bonus issues, payment of interest and dividends, supply of annual report and other information.

Rules and Regulations

The Government has framed rules under the SCRA, SEBI Act and the Depositories Act. SEBI has framed regulations under the SEBI Act and the Depositories Act for registration and regulation of all market intermediaries, and for prevention of unfair trade practices, insider trading, etc. Under these Acts, Government and SEBI issue notifications, guidelines, and circulars which need to be complied with by market participants.

Regulators

The responsibility for regulating the securities market is shared by Department of Economic Affairs (DEA), Ministry of Corporate Affairs, Reserve Bank of India (RBI) and SEBI. The activities of these agencies are coordinated by a High Level Committee on Capital Markets. The orders of SEBI under the securities laws are appellable before a Securities Appellate Tribunal.

Most of the powers under the SCRA are exercisable by DEA while a few others by SEBI. The powers of the DEA under the SCRA are also con-currently exercised by SEBI. The powers in respect of the contracts for sale and purchase of securities, gold related securities, money market securities and securities derived from these securities and carry forward contracts in debt securities are exercised concurrently by RBI. The SEBI Act and the Depositories Act are mostly administered by SEBI. The powers under the Companies Act relating to issue and transfer of securities and non-payment of dividend are administered by SEBI in case of listed public companies.

VII. ADVANTAGES OF SECURITIES MANAGEMENT AND COMPLIANCES

The Beneficiaries of Securities Management & compliances may be classified as
1. Advantages to Company

(a) Elimination of Incidences of Misstatement

Misstatement/fraud may not only be committed by company or its directors/employees etc. but also by the persons holding the securities. If the Securities Management and Compliances are undertaken as an ongoing process, it would be possible to eliminate the chances of fraud in relation to securities of the company as and when they arise.

(b) Maintenance and Updation of Records

Securities Management and Compliances ensures proper maintenance and updation of register of members, share transfer register, and share certificate register etc. Hence, dividends, bonus shares, rights shares and other entitlements relating to the securities are received by the persons entitled to them.

(c) Early Corrective Measures

It is commonly said that, “To err is human”. The persons entrusted with the responsibility of and dealing in matters relating to securities, may commit mistakes by either providing security related entitlements to wrong persons, or by entering the name of a person, who is not the shareholder, in the register of members; or removing the name of a member from the register of members even if he is holding the shares or issuing the share certificate or refund order to the person not entitled to it and so on. All such unintended mistakes committed with respect to securities can be detected and made good with the mechanism of Securities Management and Compliances.

(d) Expeditious Redressal of Investors’ Grievances

Securities Management and Compliances ensures the early detection of mistakes and frauds, proper compliance of statutory provisions and reduction in efforts involved in securities related matters due to which considerable time and energy of such human resources can be deployed in disposal of investor’s grievances. In other words, speedy disposal of investors’ grievances can be ensured with the introduction of Securities Management and Compliances.

(e) Relief from Unintended Violation of Laws

A number of prosecutions are instituted by regulatory authorities against companies and their officers in default for violation of various statutory provisions relating to securities. As the mechanism of Securities Management and Compliances ensures proper compliance of statutory provisions, unintended violation of statutory provisions can be prevented with the professional support of securities’ auditors.

(f) Reduction in Litigation

As already stated, Securities Management and Compliances ensures reduction in mistakes and speedy disposal of investors’ grievances. Therefore, litigations arising out of investors’ grievances can be prevented to a large extent with the help of mechanism of Securities Management and Compliances. Reduction in securities related litigations also save valuable time and energy of judiciary, which in turn help courts in expeditious disposal of cases.
(g) **Expeditious Disposal of Securities Related Matters**

Securities Management and Compliances assists the management of companies in complying with various statutory and procedural requirements and also acts as a pre-emptive check to monitor such compliances. Hence, securities related matters can be smoothly handled by the management of the company when the mechanism of Securities Management and Compliances is in operation.

(h) **Sustained Investors’ Confidence**

Considerable reduction in investors’ grievances, smooth processing of securities related matters and negligible chances of fraud will help restore the sustained confidence of investors which will encourage them to have interest in the securities market and also in the company resorting to the mechanism of Securities Management and Compliances.

2. **Advantages to Investor**

It is the investors’ money which is being pumped into the business of the company. It is natural that investors are concerned about the safety of their investment and also expect reasonable return on it. Securities management helps in ensuring such safety by complying with various laws through which unnecessary penalties are minimized.

3. **Regulator**

Securities management and securities audit will have a salutary effect of substantially lessening the burden of the regulatory authorities like SEBI, stock exchanges who are in charge of administration of the law by reducing the level of reduction of time in initiating prosecution against offences.

4. **Compliance officers**

Securities Audit helps compliance officers in taking proactive and corrective actions and thereby helps them in performing as efficient corporate managers.

5. **Statutory Auditor**

Securities management and compliances enables the work of statutory auditor easier due to the systematic procedures involved in the same.

VIII. **ROLE OF COMPANY SECRETARY IN SECURITIES MANAGEMENT AND COMPLIANCES**

The role of company secretary in securities management and compliances takes in the form of certifications, appearances before authorities, audit etc, which are described as below.

**Role of practicing Company Secretary (PCS)**

1. The Securities and Exchange Board of India Act, 1992/rules/regulations/guidelines/circulars
1. SEBI has authorized the practicing company secretary to appear before the Securities Appellate Tribunal as an authorized representative of an appellant.

2. Practicing Company Secretary can certify non-promoter holdings as per clause 35 of Listing Agreement in demat mode in case of the companies which have established connectivity with both the depositories.

3. PCS is authorized to issue certificate of compliance of conditions of corporate governance for companies who have listed their equity shares, debt instruments and Indian Depositories in stock exchanges.

4. PCS can issue certificate regarding maintenance of adequate security cover in respect of listed debentures by either a Practising Company Secretary or a Practising Chartered Accountant, every quarter.

5. PCS can conduct Internal Audit of Portfolio Managers.

6. PCS can issue a certificate to listed companies to the effect that all refund orders/certificates to allottees of the previous issues were dispatched within prescribed time and manner and securities were listed on the stock exchanges specified in the offer document.

7. PCS is authorized to issue a certificate to the effect that provisions of SEBI Guidelines, 2000 relating to Bonus Shares have been complied with.

2. Securities Contracts (Regulation) Act, 1956 (SCRA); and Securities Contracts (Regulation) Rules, 1957 (SCRR)

PCS role under SCRA and SCRR takes in the following forms

(i) To appear as authorized representative before the Securities Appellate Tribunal

(ii) Certificate to the effect that allotment has been made by the company on the basis approved by the Stock Exchange.


(a) PCS are authorized to issue quarterly certificate with regard to reconciliation of the total issued capital, listed capital and capital held by depositories in dematerialized form, details of changes in share capital during the quarter, and in-principle approval obtained by the issuer from all the stock exchanges where it is listed in respect of such further issued capital.

(b) PCS is authorized to carry out internal audit of depository participants.

(c) NSDL has authorized PCS to carry out Concurrent Audit in case of Demat Account opening, Control and Verification of Delivery Instruction Slips.

4. Stock exchange requirements

(a) Bombay Stock Exchange Limited

PCS are authorized to

(i) To issue Networth Certificate to be submitted by all active members including
representative members of Cash segment, Limited Trading members & Trading and/or Clearing members of the Derivatives segment of the Bombay Stock Exchange.

(ii) Certify to the effect that RTA and/or In-house Share transfer facility of Listed Companies have issued all certificates within one month of the lodgement for transfer, sub-division, consolidation, renewal, exchange or endorsement of calls/ allotment monies. This certificate is to be issued within one month of the end of each half of the financial year.

(iii) certify that equity share certificates held by promoters, etc. have been stamped “Not to be sold/transferred/hypothecated until .....” in case of listing of new equity shares issued to the shareholders of the company pursuant to the reduction of capital/BIFR order and if there are non-transferable shares in existence.

(b) National Stock Exchange Limited

PCS are authorized to do the following certifications

— Details of directors/proprietor in format C-3 of Annual Return submitted by Trading Member to the Stock Exchange

— Details of shareholding pattern/sharing pattern of corporates in format C-6 of Annual Return submitted by Trading Member to the Stock Exchange

— Details of shareholding pattern/sharing pattern of firms in format C-6 of Annual Return submitted by Trading Member to the Stock Exchange.

— Details of Dominant group of corporates in format C-7 of Annual Return submitted by Trading Member to the Stock Exchange.

— Details of Dominant group of firms in format C-7 of Annual Return submitted by Trading Member to the Stock Exchange.

— Undertaking from Relative of Persons constituting Dominant Promoter Group in format C–8 of Annual Return submitted by Trading Member to the Stock Exchange

— Undertaking from Corporates supporting Dominant Promoter Group in format C–8 of Annual Return submitted by Trading Member to the Stock Exchange

— Grant of approval for listing under clause 24(a) of the Listing Agreement – Certificate from Practising Company Secretary confirming that the entire pre-preferential holding of the allottee (mentioning the quantity) is locked in for the period starting from relevant date up to a period of six months from the date of allotment (source: www.nseindia.com)

— Grant of approval under clause 24(f) of the Listing Agreement (Amalgamation – Wholly Owned Subsidiary / other than Wholly Owned Subsidiary/Reduction of Capital under Section 100) – Certificate from Practising Company Secretary for Networth of the Company pre and post scheme under section 101, 391 and 394 of the Companies Act, 1956. (source: www.nseindia.com)

— Listing of shares arising out of Conversion of Debentures/Warrants/Notes/
Bonds into Equity Shares – Certificate from Practising Company Secretary for receipt of money at the time of allotment of Convertible Debentures/Warrants/Notes, etc. (source: www.nseindia.com)

— Listing of shares/securities issued on Preferential/Private Placement basis – Certificate from Practising Company Secretary for the following confirmations:

— The pricing of the issue along with the detailed working of the same
— The company has received the entire consideration payable prior to the allotment of shares
— The total shares under lock-in (along with the dates of lock-in and distinctive numbers) and additionally confirming that the locked in equity shares if issued in physical form have been enfaced with non-transferability condition
— The entire pre-preferential holding of the allottee (mentioning the quantity) is locked in for the period starting from relevant date upto a period of six months from the date of allotment. (source: www.nseindia.com)

— Listing of shares/securities issued on Preferential/Private Placement basis in case allotment under Section 81(3) of Companies Act – A confirmation signed by the compliance officer of the company duly counter confirmed by the Practising Company Secretary confirming that the said allotment has been made in accordance with the provisions of section 81(3) of the Companies Act, 1956. (source: www.nseindia.com)

— Certificate from Practising Company Secretary confirming securities under lock-in (the certificate should include the distinctive numbers of securities under lock-in and date from and upto which these shares are under lock-in) (source: www.nseindia.com)

(c) Other regional exchanges

Certificate to the effect that the RTA has completed all transfers within the stipulated time.

5. Foreign Exchange Management (Transfer of Issue of Securities by a Person Resident Outside India) Regulations, 2008

Practicing company secretaries are authorized to give certification which has to be accompanied by form FC-GPR, being submitted with respect to issue of shares under FDI Scheme.

Company secretary in employment

As per the listing agreement for equity, Debt instruments and Indian Depository Receipts, a Company Secretary or any other person has to be designated as compliance officer. The Company secretary as compliance officer has the following role to play.

Company Secretary of a listed company, in addition to Board Meeting and other
documentation and filing formalities are expected to do the certain activities relating to securities laws and compliance. The following are the few of the main activities

- Compliance with SEBI and Listing agreement
- Publication of financial results
- Intimations and disclosures to stock exchanges and SEBI
- Implementation of Employee Stock Option plans if any
- Cautious about takeovers
- Continuous watch on stock price movements
- Watch on insider trading
- Taking steps to prevent money laundering activities
- Carrying out necessary certifications required by stock exchanges as compliance officer of the company.

IX. SELF REGULATION

As stated earlier, there are plethora of Acts, Rules, Regulations and Guidelines relating to Securities. Inspite of it, serious securities scams have been committed and there has been an increase in investor grievances and litigations. This lays emphasis on implementation of the laws, not only in letter but also in spirit which helps in achieving the objectives of introducing the statutory provisions. Implementing the statutory provisions is not only the responsibility of the Government but also of the corporate world to ensure the proper compliance of statutory provisions. The corporate world should not treat the compliance as burden on it but should be self-motivated to ensure the compliances of statutory provisions in spirit.

Furthermore, in the era of liberalization and globalization, government has accepted the policy of rule by exception. As a consequence, the concept of certification has been introduced in many areas where relaxation has been made. Various procedural requirements have been simplified and greater confidence in relation to compliance has been posed on the corporate world itself. The concept of self-regulation is touching the new heights. The self-regulation in securities related matters can be achieved with a comprehensive mechanism of Securities Audit. Securities audit ensures self-regulation and compliance of statutory provisions governing securities related matters. Securities audit by experienced and knowledgeable company secretary in practice can ensure the path of professional discipline in the corporate world.

Securities Audit is a mechanism relieving the company and its directors from the consequences of unintended non-compliance by timely corrective actions.

There are several penal provisions in the Companies Act, 1956, Securities and Exchange Board of India Act, 1992, Foreign Exchange Management Act, 1999, Securities Contracts (Regulations) Act, 1956 and other securities related laws. As securities audit ensures the timely and proper compliances of all statutory provisions and early detection of errors and frauds, it provides trustworthy mechanism relieving the company and its directors from the consequences of unintended non-compliances of statutory provisions. Securities audit is also a powerful tool for proper
It is also a mechanism for self-regulation by companies and relieves the management, directors and officers in default from the consequences of inadvertent non-compliance of various provisions relating to securities by taking timely corrective actions. It further prevents fraudulent and unfair trade practices and helps to achieve an orderly growth of capital market. It also helps the management in improving the corporate image and helps to attain good corporate governance. Securities Audit Mechanism not only protects the interest of investors but also helps companies in proper compliance and helps regulators in regulating the capital market.

The Securities Audit shall be conducted by a company secretary in practice encompassing compliance of all rules, applicable regulations, guidelines in relation to issue of securities, issue of certificates in relation to all transactions of company’s securities, physical verification of relevant records and documents and also entering qualification, if any. The company shall be at the option to either take a comprehensive Securities Audit or a transaction specific audit such as Audit under Public Issue, Takeover Code, Insider Trading Regulations or Buy-back of Securities Regulations.

X. SECURITIES MANAGEMENT & COMPLIANCES AS A RISK MANAGEMENT TOOL

Compliance demands are going to increase and require a holistic view from the organization and ongoing maintenance of compliance processes, technology and outcomes. Non compliances results in hefty penalty, which may shake the working of the organization itself. For example non compliance of listing agreement may result in a penalty which may extend upto 25 crores. Thus management of compliance risk is an essential process.

Compliance risk is the current and prospective risk to earnings or capital arising from violations of, or nonconformance with, laws, rules, regulations, prescribed practices, internal policies, and procedures, or ethical standards. Compliance risk can lead to diminished reputation, reduced customer value, limited business opportunities, reduced expansion potential, and an inability to enforce contracts.

Securities management & compliances helps in complying with various legislations such as SEBI Act, SCRA, Depositories Act, listing agreement, certain important provisions of Companies Act, SEBI rules, Regulations, Guidelines, Rules and regulations of depositories etc. It has a major contribution to risk management as it is the major aspect of managing compliance risk.

LESSON ROUND-UP

The four main legislations governing the securities market are: (a) the SEBI Act, 1992 (b) the Companies Act, 1956, (c) the Securities Contracts (Regulation) Act, 1956, and (d) the Depositories Act, 1996.

The concept of Securities Management and Compliances thus signifies and includes in its ambit examination, verification or checking of registers, records, forms, returns and documents relating to securities issued by a company and
certification of timely and proper compliance of all statutory provisions related to securities applicable to a company.

Securities Management and Compliances has several advantages to Company, investor, regulator, auditor, financial institutions etc.

The role of company secretary in securities management and compliances takes in the form of certifications, appearances before authorities, audit etc.

**SELF-TEST QUESTIONS**

*(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation)*

1. Describe and significance and advantages of securities management and compliances.
2. Explain the role of Practising company secretary in securities management and compliances.
3. Describe securities management and compliances as a risk management tool.

Students are advised to attempt at least one Test Paper from Test Papers 3/2009, 4/2009 and 5/2009 i.e. either Test Paper 3/2009 or Test Paper 4/2009 or Test Paper 5/2009 and send the response sheet for evaluation to make him/her eligible for Coaching Completion Certificate. However, students may, if they so desire, are encouraged to send more response sheets including Test Paper 1/2009 and 2/2009 for evaluation.

While writing answers, students should take care not to copy from the study material, text books or other publications. Instances of deliberate copying from any source, will be viewed very seriously.
**WARNING**

It is brought to the notice of all the students pursuing Company Secretaryship Course that they should follow strict discipline while writing response sheets to various Test Papers appended at the end of this Study Material. Any attempt of unfair means by students in completing the postal coaching by way of submitting response sheets in different handwritings or by way of copying from the study material/suggested answers supplied by the Institute or from the answers of the students who have already completed the course successfully, etc., will be viewed seriously by the Institute. Students are, therefore, advised to write their response sheets in their own handwriting without copying from any original source.

Student may note that use of any malpractice while undergoing postal or oral coaching is a misconduct as per certain provisions of Company Secretaries Regulations and accordingly the registration of such students is liable to be cancelled or terminated.
1. (a) Distinguish between due diligence and audit. (8 marks)
    (b) Write a brief note on due diligence on mergers, amalgamations and acquisitions. (8 marks)

2. Write short notes on
   (i) Private placement. (5 marks)
   (ii) Promoters’ contribution and lock-in requirements. (6 marks)
   (iii) Reservations for Retail Institutional Investors. (5 marks)

3. (a) What are the requirements with respect to Debenture Trustee under Chapter X of SEBI (DIP) Guidelines? (8 marks)
    (b) What are the obligation of the issuer, lead merchant banker under SEBI (Issue and Listing of Debt Securities) Regulations, 2008? (8 marks)

4. (a) Explain the requirements regarding public announcement under SEBI (SAST) Regulations, 1997. (10 marks)
    (b) What are the different disclosures under SEBI (SAST) Regulations, 1997? (10 marks)

5. (a) What are the general features of joint venture? (8 marks)
    (b) Explain the preliminary considerations for a joint venture. (8 marks)

6. (a) Briefly explain about overseas investment by proprietorships concerns/unregistered partnership. (8 marks)
    (b) Explain about the scope of legal due diligence. (8 marks)

7. (a) What are the risks on trading in debentures? (8 marks)
    (b) Explain the process involved in issue of Indian Depository Receipts. (8 marks)
1. (a) What is the significance of compliance management? (8 marks)
(b) What are the objectives of Secretarial Audit? (6 marks)
(c) Explain about the scope of securities management and compliances. (6 marks)

2. Write short notes on
   (i) Particulars of charges. (5 marks)
   (ii) MCA Portal (5 marks)
   (iii) Compliance with Spirit of Law. (6 marks)

3. (a) What are the elements of an effective compliance management programme? (8 marks)
(b) What are the approaches followed by compliance solution providers? (8 marks)

4. (a) Explain about the social responsibility of the Secretarial Auditors. (8 marks)
   (b) As Secretarial Auditor what are the compliances to be looked into regarding issue and transfer of shares to non-residents? (8 marks)

5. (a) What are the possible hurdles in carrying out a legal due diligence and what are the remedial actions for the same? (10 marks)
   (b) What is the role of company secretary in legal due diligence. (6 marks)

6. (a) What is the process involved in corporate compliance management. (8 marks)
   (b) What is the role of company secretary in corporate compliance management. (8 marks)

7. (a) What is the scope and importance of search/status reports. (8 marks)
   (b) Write short note on verification of documents relating to charges. (8 marks)
TEST PAPER 3/2009
(Based on entire Study Material)

Time allowed : 3 hours Maximum marks : 100

Note: Attempt any SIX questions including Question No. 1 which is COMPULSORY.

1. (a) State with reasons whether the following statements are True or False
   (i) Companies proposing to issue IDRs need not be a listed Company.
   (ii) PAN number is mandatory to open a DP account
   (iii) IPO grading has been made Mandatory
   (iv) A promoter or every person having control over a company shall, within 30 days from the financial year ending March 31, as well as record date of the company shall disclose the number and percentage of shares held by him under SEBI (SAST) Regulations, 1997.
   (v) Reporting of Foreign Direct Investment is made in form FC-GPR.  
       (2 marks each)

   (b) Critically examine the following:
       (i) Cultural differences are to be addressed at the time of merger/amalgamation.
       (ii) Companies issuing GDR has to comply with SEC Regulations.  
           (5 marks each)

2. (i) Choose the appropriate answer.

   (a) Rights Issue (RI)
       (i) is when a listed company which proposes to issue fresh securities to its existing shareholders as on a record date.
       (ii) conveys special rights for equity shareholders
       (iii) brings preferential rights to certain shareholders
       (iv) None of the above.

   (b) The draft prospectus is filed with ...............through Merchant Banker.
       (i) ROC
       (ii) DGFT
       (iii) SEBI
       (iv) Regional Director.

   (c) When an acquirer company does not offer the target company the proposal to acquire its undertaking but silently and unilaterally pursues efforts to gain control against the wishes of existing management, it is called.............
       (i) Friendly takeover
(ii) Hostile Takeover
(iii) Takeover through consenses
(iv) None of the above
(d) The company is required to file shareholding pattern with the Exchange on a quarterly basis, within ………from the end of each quarter
(i) 21 days
(ii) 30 days
(iii) 45 days
(iv) 60 days
(e) Corporate actions are……………………
   (i) actions taken by corporates
   (ii) benefits given by a company to its members
   (iii) actions taken on behalf of aggrieved investors by corporates
   (iv) None of the above
(f) Issue of GDRs are mainly governed by …………
   (i) Foreign Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme 2003.
   (ii) Companies Act, 1956
   (iii) Depositories Act, 1996
   (iv) Depository Rules (1 mark each)
   (ii) Describe the process involved in the issue of GDRs. (6 marks)
   (iii) Write short notes on Disclosure on pledged shares by promoters. (4 marks)

3. (a) State with reasons whether the following actions of ABC Limited, are right or wrong.
   (i) The Company has proposed a bonus issue when it has defaulted in the principal and interest amount of fixed deposits.
   (ii) The Lead Merchant Banker has accepted to act as Registrar to an issue and to handle post issue responsibilities.
   (iii) The company has altered its articles of association after passing Special Resolution at a General Meeting.
   (iv) The company has kept its register of members and debenture holders at its corporate office which is situated in the same city where the registered office is situated.
   (v) The Company does not generally send any document to the members by certificate of posting or registered post. (2 marks each)
   (b) Describe the importance of due diligence. (6 marks)

4. (a) Fill in the Blank spaces with appropriate words
(i) Due diligence is often undertaken during the procurement process to ensure that risks are uncovered.

(ii) Public issues can be further classified into .......... and ............... .

(iii) At least ..........% of post issue paid up capital has to be contributed by the promoters.

(iv) .......... is the risk that an issuer of a bond may be unable to make timely payment of interest or principal on a debt security.

(v) For the redemption of the debt securities issued by a company, the issuer shall create ............... in accordance with the provisions of the Companies Act, 1956.

(vi) A ................. is made by the acquirer through a merchant banker, primarily disclosing his intention to acquire shares of the target company from existing shareholders by means of an open offer.

(b) What transactions are exempted from public announcement? (10 marks)

5. (a) Explain the need and scope of share transfer audit? (8 marks)
    (b) As a secretarial auditor, prepare a check list with respect to scrutinizing e-form-2? (8 marks)

6. (a) What are the various documents involved in the issue of GDRs? (8 marks)
    (b) What are the important clauses to be covered in a joint venture agreements? (8 marks)

7. (a) What is the process involved in legal due diligence? (8 marks)
    (b) What are the elements of an effective compliance management programme? (8 marks)
1. (a) Choose the appropriate answer.
   (a) Indian Depository Receipt means any instrument in the form of a depository receipt created by ……………………
      (i) Overseas Depository
      (ii) Depository Participant
      (iii) Domestic Depository in India
      (iv) None of the above

   (b) Foreign investment can be in the form of…………..
      (i) Technical Collaboration only
      (ii) Financial Collaboration only
      (iii) Technical and/or financial collaboration
      (iv) MOU

   (c) Foreign Investment which does not qualify under Automatic route…
      (i) Will have to be cancelled and refunded
      (ii) is prohibited
      (iii) has to go for Government approval.
      (iv) None of the above.

   (d) Investment Outside India is regulated by
      (i) Foreign Exchange Management (Transfer or Issue of any Foreign Security) Regulations, 2004
      (ii) Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000
      (iii) Listing Agreement
      (iv) None of the above.

   (e) It is desirable that the compliance management process is so designed that it is able to generate ……………..for secretarial and legal data providing the key information
      (i) a complete MIS Report
      (ii) a compliance chart
      (iii) data analysis
      (iv) None of the above.

   (f) Dematerialisation is the process of conversion of…………. in-to electronic balances
      (i) Physical Shares
      (ii) Bank Account
      (iii) Materials
(iv) None of the above. (1 mark each)

(b) Explain the compliances with respect to constitution of Audit Committee under Clause 49 of listing agreement? (6 marks)

(c) Explain about acquisition of foreign company through bidding or tender process. (8 marks)

2. (a) Critically examine and comment on the following
   (i) Due diligence is an Audit
   (ii) Public announcement is not required for inter-se transfers (5 marks each)

   (b) Write short notes on prohibited sectors for foreign investment. (6 marks)

3. (a) What are the requirements under clause 49 on the composition of the Board? (8 marks)

   (b) Write a short notes on overseas investment by registered trust/Society? (8 marks)

4. (a) State with reasons whether the action of XYZ Limited (an SSI) is correct.
   (i) XYZ Limited employed a practicing company secretary, who is also an ICWAI as its cost auditor.
   (ii) It has a foreign holding of 60% in its share capital.
   (iii) It passed a special resolution for changing its object clause of Memorandum of Association but has not filed e-form 23 for 6 months from the date of passing the Special Resolution.
   (iv) The Company being a listed company, has 75% of promoter directors on its Board. (2 marks each)

   (b) What are the advantages of data room? Explain the concept of virtual dataroom. (8 marks)

5. (a) What are the disclosures to be made in the Directors’ Report with respect to ESOP scheme of a company? (8 marks)

   (b) Write a short note on reservation for retail individual investor with examples. (8 marks)

6. (a) Write a concept and procedure for proportionate allotment of securities? (6 marks)

   (b) Write a short notes on
      (i) E-IPO (5 marks)
      (ii) Basis of allotment (5 marks)

7. (a) Write any three important event based intimations that are required to be given to the stock exchange. (8 marks)

   (b) Describe the provisions of listing agreement with respect to minimum holdings. (8 marks)
TEST PAPER 5/2009
(Based on entire Study Material)

Time allowed: 3 hours  Maximum marks: 100

Note: Attempt any SIX questions including Question No. 1 which is COMPULSORY.

1. (a) Choose the appropriate answer.
   (a) Intimation to be given to the Company Law Board in respect of any default made by the company in repayment of any deposits from small depositors has to be made………. from the date of default.
      (i) Within 60 days
      (ii) Within 45 days
      (iii) Within 30 days
      (iv) Within 7 days
   (b) Transfer of physical shares has to be made through execution of form…..
      (i) 7B
      (ii) 7A
      (iii) 24AA
      (iv) None of the above
   (c) For safer transfer of dematerialized securities………………..has to be preserved carefully.
      (i) Cheque book
      (ii) Monthly statements
      (iii) Delivery instruction slips
      (iv) None of the above.
   (d) All companies listed on stock exchanges are required to do the processing of share transfers and effect transfers in accordance with the provisions ………………………
      (i) of the Companies Act, 1956, Listing Agreement and the Guidelines issued by SEBI.
      (ii) Companies(issue of Share certificate) Rules 1960
      (iii) Companies Act, 1956
      (iv) Listing Agreement
   (e) Practicing Company Secretary will be attracting…………….., for any false statement in any material particular or omission of any material fact in the Compliance Certificate.
      (i) the penal provisions of Section 628 of the Companies Act, 1956
      (ii) provisions of Company Secretaries Act, 1980
      (iii) SEBI Act, 1992
      (iv) None of the above.
(f) A Search report prepared by the Company Secretary in Practice enables …………….. to evaluate the extent upto which the company has already borrowed moneys and created charges on the security of its movable and/or immovable properties.

(i) the Bank/Financial Institution
(ii) Investors
(iii) Depositories
(iv) Stock Exchange

(1 mark each)

(b) Draft a check list for an acquirer company who proposes to take over another company. (8 marks)

(c) Draft a compliance check list in respect of rights issue of a listed company. (6 marks)

2. (a) (i) ………………. due diligence aims at the assessment of the functional operations of the target company.

(ii) In due diligence NDA stands for ………….

(iii) A ………………… is an issue of shares or of convertible securities by a company to a select group of persons under Section 81 of the Companies Act, 1956 which is neither a rights issue nor a public issue.

(iv) The company has to obtain IPO Grading from atleast …………. and the disclosures of all grades obtained have been disclosed in the prospectus/red herring prospectus as the case may be.

(v) A tradable form of a loan/debt is normally termed as …………..

(vi) In a ………………. merger two or more companies are complementary to each other, get merged. (1 marks each)

(b) When is an acquirer required to make a public announcement and what are its contents? (10 marks)

3. (a) Write a descriptive note on regulatory framework for issue of IDRs. (8 marks)

(b) What are the advantages of securities management and compliances. (8 marks)

4. (a) Describe the procedure of operation of escrow account under SEBI (SAST) Regulations 1997. (8 marks)

(b) What transactions are exempted from public announcement? (8 marks)

5. (a) Fill in the Blanks

(i) In terms of Clause 47 of Listing Agreement a Company is required to appoint the ……………. to act as Compliance Officer who will be responsible for monitoring the share transfer process and report to the Company’s Board in each meeting.

(ii) A company shall, within …………. hours of conclusion of the Board or
Committee meeting at which the financial results were approved, publish a copy of the financial results which were submitted to the stock exchange in at least one English daily newspaper circulating in the whole or substantially the whole of India and in one daily newspaper published in the language of the region, where the registered office of the company is situated.

(iii) ............ Policy is non-mandatory requirement of listing agreement.

(iv) The legal framework for a depository system has been laid down by the ............

(v) Foreign Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme 2003 regulates the issue of ............

(vi) Indian Company has to report the particulars of foreign inward remittance within ........... days of its receipt. (1 marks each)

(b) Write short notes on

(i) Application Supported by Blocked Account (5 marks)

(ii) Foreign Indirect Investment (5 marks)

6. (a) What are the various parties involved in the issue of GDRs? (8 marks)

(b) Explain intellectual property due diligence. (8 marks)

7. (a) Describe the significance of search report. (8 marks)

(b) Describe the compliances by Merchant Banker with respect to post issue monitoring report in an IPO. (8 marks)
1. (a) State, with reasons in brief, whether the following statements are correct or incorrect:

(i) The issuer and merchant banker need not ensure that the security created to secure the debt securities is adequate to ensure 100% asset cover for the debt securities.

(ii) A private placement is an issue of shares or convertible securities by a company to a select group of persons under section 81 of the Companies Act, 1956 which is neither a rights issue nor a public issue.

(iii) A 'takeover bid' is an offer addressed to each shareholder of a company, whose shares are not closely held, to buy his shares in the company at the offered price within the stipulated period of time.

(iv) As per clause 49 of the listing agreement in respect of good corporate governance, a director shall not be member in more than 20 committees or act as chairman of more than 10 committees across all companies in which he is a director.

(v) A company can deliver the share certificate at any time after receiving the application for registration of transfer as per the Companies Act, 1956. (2 marks each)

(b) Critically examine and comment on the following:
(i) All preferential issues by the listed companies should be approved by
the shareholders’ resolution in the meeting of shareholders.

(ii) A depository participant is the agent of the investor in the depository
system providing the link between the company and investor through
the depository.  (5 marks each)

2. (a) Choose the most appropriate answer from the given options in respect of
the following:

(i) Public issue is not governed by the —
   (a) Companies Act, 1956
   (b) Foreign Exchange Management Act, 1999
   (c) Payment of Bonus Act, 1965
   (d) Securities Contracts (Regulation) Act, 1956.

(ii) In case of underwriting of rights issue, if minimum subscription is not
   received, the entire subscription should be refunded within —
   (a) 45 days
   (b) 60 days
   (c) 42 days
   (d) 30 days.

(iii) A down stream merger occurs when —
   (a) There is a merger of parent company into its subsidiary company
   (b) There is a merger of subsidiary company into its parent company
   (c) There is a merger of a healthy company with a financially weak
       company
   (d) There is a merger of a subsidiary company into its parent
       company where the parent company owns substantially all of the
       shares of the subsidiary company.

(iv) 'Overseas Custodian Bank' means a banking company which is
   established in a country —
   (a) Inside India
   (b) Outside India
   (c) Inside as well as outside India
   (d) Either inside or outside India.

(v) If a company or any other person contravenes any provision of the
    rules for which no punishment is provided under the Companies
    (Issue of Indian Depository Receipts) Rules, 2004, the company and
    every officer in default shall be punishable with fine which may
    extend to —
    (a) Equal the amount of IDR issue
    (b) Twice the amount of IDR issue
(c) Thrice the amount of IDR issue
(d) Four times the amount of IDR issue.

(vi) Payment of foreign technology collaboration by Indian companies under the FEMA regulations are allowed under automatic route subject to the limitation of the lump sum payments not exceeding —
   (a) US $5 million
   (b) US $10 million
   (c) US $2 million
   (d) US $3 million.  

(b) Write a note on 'intellectual property due diligence'.  (4 marks)

(c) Distinguish between the following:
   (i) 'Due diligence' and 'audit'.
   (ii) 'American depository receipts (ADRs)' and 'global depository receipts (GDRs)'.

3. (a) As a Practising Company Secretary, you have been asked to carry out the due diligence of XYZ Ltd. for a possible acquisition of the controlling interest from the owners of the said company. Explain briefly the possible hurdles that may occur while carrying out the due diligence and the steps needed to overcome such hurdles. (6 marks)

(b) Anshul Power Generation Ltd. is contemplating setting-up an audit committee as part of good corporate governance. As a Company Secretary of the company, advise the company on the constitution, composition, quorum and the role of audit committee. (6 marks)

(c) Explain the following terms used in due diligence report —
   (i) Deal breakers
   (ii) Deal diluters. (2 marks each)

4. (a) Re-write the following sentences after filling-in the blank spaces with appropriate word(s)/figure(s):
   (i) Shares issued under an Employee Stock Purchase Scheme (ESPS) are subject to lock-in for a minimum period of __________ year from the date of allotment.

   (ii) The credit rating is required to be obtained from at least ________ registered credit rating agencies under the SEBI (Public Offer and Listing of Securitised Debt Instruments) Regulations, 2008.

   (iii) A public limited company is required to appoint the Company Secretary to act as compliance officer under clause __________ of the listing agreement.

   (iv) As per clause 49 of listing agreement, at least ________ of the Board should include independent directors where chairman of the Board is a non-executive director.
(v) An American Depository Receipt (ADR) is a ________ denominated form of equity ownership in the form of depository receipts in a non-US company.

(vi) Pre-issue paid-up capital and free reserves of the issuing company should be at least__________ under the Companies (Issue of Indian Depository Receipts) Rules, 2004 for the issue of IDRs. (1 mark each)

(b) As a Practising Company Secretary, you have been appointed as secretarial auditor of Lilly Ltd. Explain briefly how you would undertake the process of secretarial audit. (10 marks)

5. (a) Sanjay is a Practising Company Secretary and has been engaged as internal auditor of the operations of depository participants. Do you feel it is mandatory on the part of the depository participants to appoint an internal auditor? What should be the contents of the internal audit report? (8 marks)

(b) As a Practising Company Secretary, you have been assigned to work out preliminary considerations for setting-up a joint venture. State the preliminary considerations to be taken care of in this regard. (4 marks)

(c) A depository participant is required to enter into two important agreements in the course of trading in dematerialised securities. Explain. (4 marks)

6. (a) Anmol Milk Products Ltd. is planning to expand its operation by financing Rs.75 crore through a term loan from the IDBI Bank Ltd. The company has applied for a term loan and the assets of the company will be mortgaged to the lending bank as security.

The bank has approached you, being a Practising Company Secretary, to furnish a certificate in respect of necessary powers of the company and its directors to enter into an agreement. State the general points to be kept in mind for furnishing such a certificate. (6 marks)

(b) Enumerate the points to be checked by a Secretarial Auditor in respect of the Air (Prevention and Control of Pollution) Act, 1981. (6 marks)

(c) Describe the role of a Company Secretary in Practice in securities management and compliances under the SEBI Act, 1992 and its regulations. (4 marks)

7. (a) Write short notes on any two of the following:

(i) Takeover defences

(ii) Appraisal of register of members/debentureholders

(iii) Risks on trading in debt securities. (4 marks each)

(b) Distinguish between any two of the following:

(i) ‘Dematerialisation’ and ‘rematerialisation’.

(ii) ‘Financial collaboration’ and ‘technical collaboration’,

(iii) ‘Depository’ and ‘depository participant’. (4 marks each)
8. Critically examine and comment on **any four** of the following:

(i) A key step in any due diligence exercise is to develop an understanding of the purpose for the transaction.

(ii) In case of preferential issue of shares by listed companies, valuation is to be done by an independent qualified valuer.

(iii) Under the Employee Stock Option Scheme, the companies have freedom to determine the exercise price.

(iv) A conglomerate merger involves coming together of two companies in different industries.

(v) Securities held in a depository account can be pledged or hypothecated against a loan, credit or guarantee availed of by the beneficial owner of such securities. *(4 marks each)*