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NATIONAL LAW UNIVERSITY, DELHI

LL.M. Degree Programme, II-Semester (Batch of 2018)

End-Semester Examinations, April - 2019

Paper: Advanced Corporate Law

Time: 3:00 Hours | Total Marks: 50

Instructions:

1. The duration of the examination is three hours and is for 50 marks. The first question is of 24 marks, the second question is of 16 marks and the third is of 10 marks. All the parts of a question carry equal marks.
2. All questions are compulsory.
3. Examinees can use printed matter during the examination for reference. No hand written matter in any form is allowed.
4. No clarification shall be sought on the question paper.
5. Do not write anything on the question paper except your roll no.

Q1. Ranjit Paul and his wife, Sanyukta Paul, form a company RamSan Decorators Private Limited (hereafter referred to as Company in the question) for the purpose of doing business as interior decorators. The authorized equity share capital of the Company was Rs. 5 crores out of which Rs 60 lakhs (sixty thousand shares of Rs. 100 each) was as the subscribed and paid up equity capital, with Ranjit and Sanyukta's holdings being in the ratio of 3:1. Sanyukata's father Ram Dhari acted as an angel investor in this venture of his daughter and son-in-law and subscribed to non-cumulative participative preference shares worth Rs.2 crores (2 lakh shares of Rs.100 each) which had a right to preferential dividend of 1% per annum and were redeemable after 20 years, with a right to a seat at the Board till their redemption. The Articles of the Company were broadly as per Table A of Schedule I of the Companies Act, with the differences being specified here where needed.

On the basis of above given facts and additional facts as indicated in specific questions, answer any three of the following questions:

a) The Board of the Company, comprising of the husband and wife and Ram Dhari, taking into account the need for additional funds for its smooth working, decides to raise debt finance. Because of fluctuating financials of the company, it was difficult to get banks or finance companies to lend on agreeable terms. Thereafter, the company decided to issue 5000 optionally convertible debentures of Rs. 5000 each to Ranjit Paul, with interest payable at 15% annually, redeemable after 10 years if not converted. The conversion ratio was to be determined at the time of conversion as per an agreed formula provided by a reputed firm of chartered accountants, taking into account the principles to be used for determining the fair value of the Company's shares. Some of the debentures were for fresh money bought into the Company by Ranjit, and some were in lieu of the remuneration due to him as a professional interior designer for work already rendered but not paid for due to losses sustained in the initial operating years. The understanding being, but not mentioned in the debenture deed, that if the Company was not in a position redeem, the debentures would either be converted or fresh ones issued in lieu of them on same terms.

Three years after the issuance of debentures, separation proceedings start between Ranjit and Sanyukta. As a corollary to the other disputes between them, Sanyukta now contends that the Board did not have the power to issue the debentures (the Articles being silent on them) and therefore the said debentures could not be converted into equity shares of the Company.
Ranjit approaches you for guidance and an appropriate response. Advise him.

b) After the divorce proceedings start between Ranjit and Sanyukta, Ranjit wants to redeem the preference shares issued to his father-in-law Ram Dhari, though only five years have elapsed since their issuance. Ram Dhari opposes it, forcing Ranjit to look into the option of reducing the share capital by paying of the preference shares at a fair value. Advise Ranjit on the feasibility of the said measure and steps preparatory to it which he may need to take after taking into account the facts narrated in (a) above.

c) Subsequent to the initiation of divorce proceedings between Ranjit and Sanyukta, Sanyukta communicates to Ranjit that the Company should not take any new orders for work as she did not have confidence in Ranjit's competence and ethics, which in her view would affect her own reputation and thereafter her ability to start on her own after the Company's dissolution, which in her thought was inevitable as well as desirable to get her and her father's fair share of gains.

A vendor of the Company introduces Ranjit to a prospective new client. The MD of the client had earlier in his prior employment had given and overseen the execution of work orders given to the Company and had been satisfied with quality and professionalism displayed in its execution. Ranjit negotiates with the client, using the Company's client list and prior work done by it and him to become eligible for being considered for the work and his suitability for its award to him. He, thereafter, pursuant to prolonged negotiations, of which Sanyukta had an inkling, gets an order to do the interiors of the new client's upcoming office block of 2 lakh square feet which he seeks to execute through his new company Ranjit Decorators Private Limited. Sanyukata sues Ranjit and the new company to account for the profits. The parties agree to an arbitration and appoint you as one. Decide on the issues involved in in the dispute.

d) In the fact situation narrated in {c} above, Sanuykta and her father, use their majority on the Board to prevent the declaration of any dividends to the preference shares for 3 years continuously and thereafter gang up to oust Ranjit from the Board when the negotiations with the client had still to start, and thereafter terminate his engagement with the Company as a designer/decorator. Ranjit approaches you for advise and legal opinion as to the course of conduct to be pursued by him and his options. Advise him.

Q2. Arijit Basu and his son Dipankar Basu were the shareholders of a company engaged in the pharmaceuticals business named Partha Medications Private Limited {hereafter referred to as Partha Co.). Partha Co. was a stockist, wholeseller and retailer of medicines, including acting as supplier to hospitals. During the course of business they encountered difficulty in selling drugs/medicines to some prominent hospitals and nursing homes, charitable or for profit, in western UP which they found had been promoted by a certain community. Enquiries revealed that the said establishments dealt almost exclusively with Khemchand Pharmaceuticals Ltd{ hereafter referred to as Khemchand Co.}. Arijit went through the public records available on this competitor with the Registrar of Companies and otherwise and were impressed with its balance sheet, including its profitability. Thereafter via an investment banker a proposal for merger was sent which was accepted after prolonged negotiations. The merged entity was named Partha Pharmaceuticals and Medications Ltd.(hereafter referred to as Company), with Arijit continuing as managing director of the merged entity. After a few weeks it became evident that the balance sheet of Khemchand Co. was not as rosy as shown and the merged entity struggled with debt repayments and manufacturer/supplier notices for five years before filing for insolvency.

Based on the above and the facts narrated in the individual questions, answer any two of the questions given below:

a) The balance sheet of Khemchand Co. had inflated the profits and also mysteriously payed taxes on it. The charitable hospitals to which it used to supply the medicines were usually in default and other medical establishments of the same community would give their custom to Khemchand Co. taking into account the accommodation provided by it to the charitable hospitals run by the community. But Khemchand Co. would show the sales to the community hospitals as debt due to it and never wrote off the amount even when the debts became time-barred. All of the medicines in its warehouses were shown at the cost of acquisition even when it was found that substantial part of the supplies were beyond their expiry date, hence virtually worthless. The auditor had certified the accounts as reflecting the true state of affairs without any qualifications which could have bought this to the notice of the outsiders. In the liquidation proceedings, the liquidator seeks damages from the auditor for the negligence which resulted in overvaluation of the business of Khemchand Co. and thus a higher price being paid for its shares and the loss suffered by the creditors of the Company for relying on the audit report.

   State Bank of India, one of the creditors seeks your legal opinion as to the feasibility of any recovery in the event of pursuing this course of action.

b) Arijit Basu and Dipankar Basu, in the merger negotiations had provided that the Company had a right to recover the excess amount paid for the business from the directors of Khemchand Co. if the profits and balance sheet were not reflective of reality. However, in the months preceding the start of insolvency proceedings, the father son duo thought that the directors of Khemchand Co. were needed for recovering the dues from the defaulting hospitals as they had their contacts within the community managing the hospitals who would exert pressure on the management of the said hospitals to pay or else get compensatory high margin business from the non-charitable hospitals. Pursuant to this belief of theirs, they passed a board resolution exonerating the directors of Khemchand Co. of their liability.

   The liquidator now accuse the duo of gross incompetence and dereliction of duty in ending claims against directors of Khemchand Co. and asks them to account for the loss due to it. Advise Arijit and Dipankar on their potential liabilities and possible defences.

c) During the course of forensic audit of the Company, engaged in by the liquidator pursuant to the request by the creditors, it was found that for the last three years Arijit Basu was hospitalized for an ailment which rendered him unfit to carry on his duties. Despite this, he still carried on as an MD of the company and drew regular salary and was paid bonuses. To pay for his hospital expenses, the company surrendered its tenancy rights to an warehouse owned by the Basu family which promptly sold it as unencumbered property to raise money for treatment in New York. The liquidator approaches you to understand if there is a case which can be pursued against Mr. Arijit Basu and others.

Q3. Write short notes on any two of the following

a) The tests to determine the conditions in which the corporate veil be lifted.

b) Winding up of a company on the ground that it is just and equitable to do so.

c) The justifications for the rule in Foss vs. Harbottle and the exceptions to it.