

NATIONAL LAW UNIVERSITY, DELHI

LL.M., Semester-I (Batch of 2021)

End Semester Assessment, December-2021

Paper: Advanced Corporate Law

Total Marks: 50

Instructions:

1. Mail your assignments only to **submissions.llm@nludelhi.ac.in**
2. All questions are compulsory.
3. This is an open book exam. Students are free to consult their class notes as well as assigned reading materials.
4. No clarification shall be sought on the question paper.
5. Mention **ONLY** your Name, Roll No. and Subject Paper on the Cover/First page. Start writing your answers from the next/second page only. **Do not** mention your name and roll no on any other page.
6. All parts of a question carry equal marks. Question 1 is of 12 marks while Question 2 and 3 are of 18 and 20 marks respectively.

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- 1) Bhalla group of companies were in the pharmaceutical business. The business was managed by a complex structure so as to preserve the control of the Bhalla family over the group companies as well as to raise capital for business conveniently, reduce tax incidence as well as risks and potential liabilities. The intellectual properties over the drugs and every other intellectual properties of the group, including the brand names under which the drugs were sold, patents and licenses (from third parties) for various chemicals were held by Ajax BVI, a company incorporated in British Virgin Islands, whose entire share capital was owned by investment companies, whose entire share capital in turn was owned or controlled by the Bhalla family. The active pharmaceutical ingredients (API) used for the manufacture of the drugs were made by Ajax Pharmaceuticals Ltd., a publicly listed company in India, with manufacturing facilities in an export processing zone. Bhalla family owned or controlled 45% of the shares of Ajax Pharmaceuticals Ltd. The products of Ajax Pharmaceuticals Ltd. was bought by Ajax Trading Co. Ltd., a company incorporated in Singapore and majority of the shares of which was owned or controlled by the Bhalla family, which thereafter sold the API to the different Bhalla group companies in different parts of the world, to produce and sell drugs under different brands under license or sub-license from Ajax BVI. One of the companies in the Bhalla group, Ajax Latino Pharma Ltd., was incorporated in Trinidad and Tobago and did business in Latin American countries. Research by some medical colleges in the last decade of the twentieth century seemed to suggest a causal link between some of the drugs manufactured and sold by the Bhalla group of companies and an allergic reaction which the group initially ignored. In 2014, a research conclusively proved that there was a linkage between these allergic reactions and the seizures, nervous breakdowns and even deaths of some patients. The families of victims in Brazil moved against Ajax Latino Pharmaceuticals Ltd. in a Brazilian court. The decree of the Brazilian court was unsatisfied as the defendant company became insolvent as it was thinly capitalized. The families seek to move the Indian courts for the satisfaction of their claims. They seek your advice on the Indian law and the sustainability of their claims in the Indian courts. Advise them. **(2500 words)**

- 2) Arijit Basu and his son Dipankar Basu were the shareholders of a company, Partha Medications Pvt. Ltd. (hereinafter referred to as Partha Co.), engaged in the pharmaceuticals business. Partha Co. was a stockiest, wholeseller and retailer of medicines, including supplies to hospitals. During the course of business, they found that selling drugs and medicines to hospitals and nursing homes promoted by a certain community in the State of Uttar Pradesh was very difficult, irrespective of the fact as to whether they were for profit or were charitable institutions. Enquiries revealed that the said establishments almost exclusively dealt with Khemchand Pharmaceuticals Ltd. (hereinafter referred to as Khemchand Co.). Arijit went through the available public records on this competitor of his, including those with the Registrar of Companies and was impressed with the strength of its balance sheet, including profitability. Thereafter a proposal for merger was sent via a merchant banker, which was accepted after prolonged negotiations. The merged entity was named Partha Medications and Pharmaceuticals Ltd. (hereinafter called the NewCo), 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 was shown and the merged entity struggled with debt and found it difficult to pay its manufacturer-suppliers, many of whom fed up with delays black-listed it and gave supplies only on cash payments. After struggling for five years, the creditors filed for the insolvency of the NewCo.

Based on the above and the facts narrated in the individual parts, give advice to the party on the aspects it seeks advice: **(1500 words each)**

- a) The balance sheet of Khemchand Co. had inflated the profits and also mysteriously paid taxes on it. The charitable hospitals to which it supplied medicines were usually in default and 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. showed the sales due from the charitable hospitals of the community as debt due to it and did not write off the debt even when it became time barred. All of the medicines in its warehouses were valued in the account books on the cost of acquisition even though a lot of it 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 brought this to the notice of the outsiders. In the liquidation proceedings, the liquidator seeks damages from the auditor for the negligence which resulted in the over-valuation of the business of Khemchand Co. and thus a higher price being paid for its shares in the form of share exchange ratio and the loss suffered by the creditors of the company for relying on the audit report.

SBI, one of the creditors of the NewCo, seeks your legal opinion as to the feasibility of any recovery in the event the liquidators course of action is pursued.

- b) Arijit Basu and Dipankar Basu, in the merger negotiations had provided that the NewCo. had a right to recover the excess amount paid for the business from the directors of Khemchand Co. if the balance sheet was not reflective of the reality. However, in the months preceding the initiation of the insolvency proceedings, the father son duo thought that the directors of Khemchand Co. were needed for the recovery of dues from the defaulting hospitals as they had the goodwill of the community managing them and contacts within the influential circles of the said community. They believed that this would enable them to either persuade the charitable hospitals to honour their financial commitments or would enable them to get new high margin business from for profit establishments of the community members, without the customary discounts given to the hospitals. Pursuant to this belief of theirs, they passed a board resolution exonerating the directors of Khemchand Co. of their liability.

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

- c) During the course of forensic audit of NewCo, it was found that for the last 3 years Arijit Basu was hospitalized for an ailment which rendered him unfit to carry on his duties effectively. Despite this, he still carried on as an MD of the company and drew regular salary and paid bonuses. To pay for his medical expenses, the company surrendered its tenancy rights to a warehouse owned by the Basu family, which promptly sold it as an 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 Arijit Basu and the Basu family.

- 3) Ranjit Paul and his wife, Sanyukta Paul, form a company RamSan Decorators Private Ltd. (hereinafter referred to as RamSan) 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 the subscribed and paid up equity capital with Ranjit and Sanyukta's holdings being in the ratio of 3:1. Sanyukta'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) with a preferential dividend of 1% and redeemable after 20 years. The articles of the company were broadly as per Table A of Schedule I of the Companies Act, with differences being specified here where required.

On the basis of the given facts and additional facts as provided in the relevant part, advice/decide in the following **(1500 words each)**

- a) The board of the company comprising of the husband-wife duo and Ram Dhari, took into account the need for additional funds for the smooth working of the company and decides to raise debt finance. Because of fluctuating financials of the company, it was difficult to get banks or NBFCs to lend on agreeable terms. Thereafter, the company decided to issue 5000 optionally convertible debentures of Rs. 5000 each to Ranjit Paul, at 15% annual interest rate and 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 unsaid understanding was that if the company was not in a position to redeem the debentures, then either they would be converted or new ones would be issued in lieu of them on the same terms. Three years after the issuance of the debentures, separation proceedings started 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, though a mere 5 years have elapsed since their issuance. Ram Dhari opposes it, forcing Ranjit to look at 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 the divorce proceedings between Ranjit and Sanyukta, Sanyukta communicates to Ranjit that the company should not take any new orders for work as she does 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 she thought was inevitable and desirable to get her and her father's fair share of the gains.

A vendor of the company introduces Ranjit to a prospective new client. The MD of this potential new client had in his prior employment observed the execution of the work orders given to RanSan and was impressed with the quality and professionalism displayed. Ranji negotiates with the client, using RanSan's client list to become eligible for the work. He, pursuant to prolonged negotiations of which his wife had an inkling, gets order to do interiors of the new client's upcoming office block of 2 lakh square feet which he seeks to execute through a new company Ranjit Decorators Pvt. Ltd. Sanyukta sues her husband and the new company for profit. The parties agree to an arbitration and appoint you to do so. Decide on the issues involved.

- d) In the fact situation narrated in (c) above, Sanyukta 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 oust Ranjit from the Board when the negotiations with the client had still to start, and terminate his engagement with the company as a decorator. Ranjit approaches you for advice and legal opinion as to the course of conduct to be pursued and his options. Advise him.