# Module 1 · The Companies Act, 2013

P13 · Section A (Corporate Laws)

SM pp. 3–157 + exercise 158–172. **The heaviest module in P13: 381 marks in 7 papers, about 54 a paper.** One notes PDF per topic; this page is the map.

| Topic (PDF) | SM pp. | J23 | D23 | J24 | D24 | J25 | D25 | J26 | Total | Dec'26 |
|---|---|---|---|---|---|---|---|---|---|---|
| **1.5** Directors and KMP | 82–115 | 13 | 21 | 13 | 11 | 8 | 7 | 14 | **87** | A · 9–14 |
| **1.4** Accounts and Audit | 51–81 | 12 | 10 | – | 7 | 2 | 15 | 18 | **64** | A · 9–16 |
| **1.6** Board Meetings | 116–132 | 6 | 7 | 9 | – | 21 | 14 | – | **57** | A · 7–14 |
| **1.1** Formation and Conversion | 3–33 | 4 | 9 | 9 | 9 | – | 9 | 13 | **53** | A · 7–13 |
| **1.2** Loans, Investments, Deposits | 34–43 | – | 7 | 7 | 2 | 14 | 9 | – | **39** | A · 7–9 |
| **1.8** Compromises, Amalgamations | 141–149 | 4 | 7 | – | 7 | – | 7 | 7 | **32** | A · 7 |
| **1.9** Oppression and Mismanagement | 150–157 | 4 | – | 7 | 7 | 7 | 2 | 2 | **29** | B · 2–9 |
| **1.3** Dividends | 44–50 | 5 | 2 | – | – | – | – | 7 | **14** | B · 2–7 |
| **1.7** Inspection, Investigation | 133–140 | 4 | 2 | – | – | – | – | – | **6** | C · 0–2 |
| **Module 1** | | **52** | **65** | **45** | **43** | **52** | **63** | **61** | **381** | |

**HOW MODULE 1 IS EXAMINED (P13 ANALYSIS, 5 OCT)**

- **Q2, Q3, Q4 and Q5(a): seven 7-mark halves are Companies Act**, and the topic in each position rotates. You choose 5 of the 7 long questions, so Module 1 alone can carry most of your long-answer marks.
- **Q1 MCQs:** a **4-MCQ case set on one Companies Act area** (Board meetings 100%, mergers 80%, directors 60%, audit 60% in our model), plus **2 single Companies Act MCQs**.
- **Due back: 1.6 Board meetings** (0 in Jun'26 after 3 + 2 halves) and **1.2 deposits / inter-corporate loans** (0 in Jun'26). **Overdue:** managerial remuneration (1.5; last long Jun'23).
- **The SM is outdated in places**: OPC rules, the conversion approval authority, fraud reporting, political contributions, small company. Each pack has ⚠ boxes; write the current law with one line on the SM version.

**STUDY ORDER (2 HOURS A DAY)**

1. **1.5** Directors (12 pp) · **1.6** Board meetings (8 pp)
2. **1.4** Accounts and audit (11 pp)
3. **1.1** Formation (10 pp) · **1.2** Loans and deposits (6 pp)
4. **1.8** Mergers (6 pp) · **1.9** Oppression (4 pp)
5. **1.3** Dividends (3 pp) · **1.7** Inspection (2 pp)
6. Before each mock: every pack's **revision page + model answers**

**HOW TO USE EACH PACK**

- **Page 1** of each pack: what was asked, the prediction, the map.
- Learn the **tables and flows**; they are the answer structure.
- **Model answers** show the layout: provision → facts → conclusion, in numbered points.
- ⚠ **boxes** = where the SM is wrong or outdated. **SM WORDS** = learn word for word.
- Small grey **[SM nn]** = study-material page, to look up anything.

# M1 Mind map: the Companies Act on one page

### 1.1 Formation (53)

- public 7 / private 2–200 / OPC 1 · small company ₹10 cr / ₹100 cr
- OPC: Indian citizen, nominee, no minor (2021: residency dropped)
- RO: same city → Board · other State → special resolution + CG
- doctrines: constructive notice · indoor management (Turquand) · ultra vires
- conversions: special resolution; public → private needs CG (RD); LLP → co s.366
- s.8: licence, no dividend, ₹10 lakh–₹1 cr penalty

### 1.2 Loans and deposits (39)

- s.186: 60% (PUC+FR+SP) or 100% (FR+SP), higher → else special resolution
- interest ≥ G-sec yield closest to tenor (1/3/5/10 yrs)
- s.187: own name; nominee for the subsidiary minimum; 4 exemptions
- deposits: members 10% / public 25% / 6–36 months / DRRA 20% by 30 April
- eligible co: NW ₹100 cr or turnover ₹500 cr

### 1.3 Dividends (14)

- out of profits after depreciation; free reserves only
- from reserves: 3-yr average · 1/10 · losses first · 15% left
- separate account in 5 days · pay in 30 days · 18% interest (s.127)
- unpaid 7 yrs → IEPF (90 days, DIV-5)

**Companies Act, 2013**
Module 1

29 chapters · 470 sections · 7 schedules

≈ 54 marks a paper

### 1.4 Accounts and audit (64)

- books at RO, 8 yrs, e-form backup in India; any director inspects
- s.134: FS signed by chairperson / 2 directors incl. MD + CFO + CS · Board's report list · DRS
- auditor: Board 30 days / 1st AGM–6th AGM / ADT-1 15 days / rotation 5 or 2×5
- removal: special resolution + CG (ADT-2) · resignation ADT-3 in 30 days
- s.141 bars: debt > ₹5 lakh, relative's shares > ₹1 lakh, > 20 audits · s.144 services
- fraud s.143(12): 45 + 15 days, ADT-4 e-form

### 1.5 Directors and KMP (87)

- IDs: listed ⅓ · public ₹10 cr / ₹100 cr / ₹50 cr → 2 · woman: listed / ₹100 cr / ₹300 cr
- s.160: 14 days, ₹1 lakh, 25% · not for Govt / pvt / ballot companies
- s.161: additional till AGM · alternate 3 months abroad · nominee · casual
- remuneration: 11 / 5 / 10 / 1 / 3% · sitting fee ₹1 lakh
- removal: ordinary resolution + special notice · s.164 disqualification · s.167 vacation
- KMP: listed or ₹10 cr; one company + subsidiary · RPT s.188 + omnibus

### 1.6 Board meetings (57)

- first in 30 days · 4 a year · gap ≤ 120 days
- notice 7 days · shorter: 1 ID present or ratifies · video counts
- quorum ⅓ or 2 (round up; vacancies out; interested out; ≥ ⅔ interested → disinterested ≥ 2)
- circulation: majority; ⅓ can demand a meeting · minutes in 30 days
- audit committee: 3, majority IDs; recommendations not binding but reasons disclosed
- political contributions: Board meeting; 3 yrs old; ⚠ 7.5% cap restored 2024

### 1.8 Mergers (32)

- s.230: NCLT → meetings → ¾ in value → sanction → ROC in 30 days
- objection: ≥ 10% shares / ≥ 5% debt · dispense if 90% creditors agree
- s.233 fast track: small / holding + WOS / start-ups: 90% members, 9/10 creditors
- s.237: CG order in public interest; compensation; appeal in 30 days

### 1.9 Oppression (29) · 1.7 Inspection (6)

- s.244: 100 or 1/10 members (lower), or 1/10 capital; waiver by NCLT
- withdrawal after filing does not defeat the petition (Rajahmundry)
- Foss v. Harbottle + 6 exceptions · class action s.245
- 1.7: ROC inquiry s.206(4) · SFIO s.212 · s.213 NCLT: 100 / 1/10

# 1.5 · Board of Directors and Key Managerial Personnel P13 · Module 1

· Companies Act, 2013

SM pp. 82–115 (34 pages). **The highest-scoring topic in P13:** 87 marks in 7 papers, in every paper, with a long question in 6 of them.

| Paper | What was asked | Marks |
|---|---|---|
| Jun'23 | Q2(b) managerial remuneration case (MD 5%, others 1%) · Q3(b) minimum independent directors, unlisted vs listed | 8 + 5 |
| Dec'23 | Q2(b) omnibus approval of RPTs: conditions · Q3(a) s.180 restrictions on the Board · Q5(a) acts of a director whose appointment is invalid | 7 + 7 + 7 |
| Jun'24 | MCQs: ID threshold ₹10 crore; small shareholder ₹20,000; expert as additional director · Q4(b) AGM rejected him, Board makes him additional director: valid? | 6 + 7 |
| Dec'24 | MCQs: removal by ordinary resolution; DIN application = Rule 9 · Q3(a) **board composition case** (IDs, related director, bank nominee, woman director) | 4 + 7 |
| Jun'25 | Q1 (i)–(iv): the same board composition case as a 4-MCQ set | 8 |
| Dec'25 | Q2(a) **s.160 candidature notice**: govt company / ballot / vernacular newspaper | 7 |
| Jun'26 | Q2(b) KMP holding office in more than one company (s.203) · Q3(a) **s.160 again**, almost word for word | 7 + 7 |

**HOW IT IS EXAMINED**

- **Case questions with numbers**: "is the board properly constituted?", "how many IDs?", "is this remuneration within limits?". Learn the **thresholds table** (next page) and the **case checker** flow.
- **Repeats:** the board composition case came in Dec'24 and again in Jun'25. s.160 came in Dec'25, again in Jun'26, and is in ICMAI's MQP. Model answers are at the end of this pack.
- **The exam copies the SM here too:** Dec'23 Q2(b) and Q3(a) are SM sentences. Dec'24 Q1(iii) and Jun'24 Q1(iii) are SM exercise MCQs 46 and 45.

**DEC'26: OUR PREDICTION (A PREDICTION, NOT A PROMISE)**

Tier **A** (must prepare). Expected **9–14 marks**: a 7-mark case or theory question plus 1–2 MCQs. Our model gives it a 60% chance of being the 4-MCQ case set in Q1. Likely questions:

1. Board composition case: IDs, woman director, nominee, related director (asked 2×)
2. Managerial remuneration limits with a calculation (last long question Jun'23, so overdue)
3. Resignation (s.168) and removal (s.169) of a director (ICMAI PTP)
4. Additional / alternate / casual-vacancy director (s.161; Jun'24)

**MAP OF THIS PACK (★ = exam weight)**

1. Board structure and thresholds, s.149 ★★★
2. Appointment, rotation, s.160 notice ★★★
3. Additional, alternate, nominee, casual; small shareholders ★★
4. Disqualification, vacation, resignation, removal ★★
5. MD, WTD, manager (s.196) and KMP (s.203) ★★
6. Remuneration s.197–202 ★★★
7. Powers s.179 and restrictions s.180 ★★
8. DIN s.153–159 + KYC amendment ★
9. Loans s.185, interest s.184, RPT s.188 ★★
10. Model answers · numbers · SM MCQs

## 1 Board structure: who must be on the Board (s.149)

**WHAT IT IS** Every company is run by a Board of individual directors who act **collectively**. The Act fixes how many directors there must be, and which companies need a woman director, a resident director and independent directors. Most case questions are just these thresholds applied to the facts. [SM 82–83]

| Requirement | Rule | SM |
|---|---|---|
| **Minimum directors** | public company **3** · private company **2** · OPC **1** [SM 83] | 149(1) |
| **Maximum directors** | **15**; more by **special resolution**. The limit does not apply to Government and section 8 companies [SM 83] | 149(1) |
| **Woman director** (at least 1) | (1) every **listed** company; (2) every other **public** company with paid-up capital **≥ ₹100 crore** or turnover **≥ ₹300 crore**. A new company complies within **6 months** of incorporation. An intermittent vacancy is filled by the next Board meeting or within **3 months**, **whichever is later** [SM 83–84] | Rule 3 |
| **Resident director** (at least 1) | stayed in India at least **182 days** in the financial year [SM 84] | 149(3) |
| **Independent directors** (IDs) | **Listed:** at least **one-third** of all directors (a fraction counts as one). **Other public companies: at least 2 IDs** if paid-up capital **≥ ₹10 crore**, OR turnover **≥ ₹100 crore**, OR loans + debentures + deposits **> ₹50 crore** (on the last audited date). A higher number applies if the audit committee needs more. Intermittent vacancy: next Board meeting or **3 months**, whichever is later [SM 84] | 149(4), Rule 4 |
| **Whole-time KMP** | listed companies + public companies with paid-up capital **≥ ₹10 crore**: MD / CEO / manager (or WTD) + CS + CFO (see part 5) [SM 96] | 203, Rule 8 |

**⚠ SM SAYS TWO THINGS**

For the resident director, the SM first says "182 days in the **financial year**" (the current Act) and then "in the previous calendar year" (the old wording). Write **financial year**. [SM 84]

### Who is an independent director? s.149(6): a director other than an MD, WTD or nominee director

[SM 84–85]

a. a person of **integrity** with relevant expertise and experience, in the Board's opinion

b. is not and was not a **promoter** of the company or its holding, subsidiary or associate company, and is **not related** to its promoters or directors

c. has or had **no pecuniary relationship** with them (apart from remuneration as a director, or transactions up to **10%** of his total income) in the **2 preceding financial years** or the current year

d. no **relative** holds securities above **₹50 lakh** face value or **2%** of paid-up capital, is indebted or has given guarantees beyond prescribed limits, or has other transactions of **2%** or more of turnover or income

e. neither he nor a relative was a **KMP or employee** in the **3 preceding financial years**, or a partner or employee of its **audit, CS or cost-audit firm**, or of a legal or consulting firm with **10%**+ of its turnover from the company; does not hold **2%**+ of voting power with relatives; is not CEO or director of an NGO getting **25%**+ of its receipts from the company

f. has other prescribed qualifications. He registers in the **IICA databank** and passes its test; exempt with **10 years** as a KMP, advocate, or practising CA/CMA/CS, or in equivalent government service [SM 85–86]

### Case checker: "Is the Board properly constituted?"

**1 · KIND OF COMPANY** listed? public or private? note paid-up capital, turnover, borrowings → **2 · NUMBER** ≥ 3 public / 2 private; ≤ 15 unless special resolution → **3 · IDs NEEDED** listed: ⅓ · public with ₹10 cr capital / ₹100 cr turnover / > ₹50 cr borrowings: 2 → **4 · WHO QUALIFIES** strike out MD, WTD or functional directors, nominees, promoters, relatives of promoters → **5 · WOMAN + RESIDENT** listed / ₹100 cr capital / ₹300 cr turnover → 1 woman; 1 resident (182 days) → **6 · KMP** listed / ₹10 cr capital → MD-CEO + CS + CFO

Write the answer in the same order: **provision** → **facts** → **conclusion** for each point, then **"what the company must do"**. A worked answer is in part 10.

## 2 Appointment, rotation and the s.160 notice

### s.152: how directors are appointed [SM 86]

- If the articles name no first directors, the **individual subscribers to the memorandum** are deemed first directors; in an OPC, the individual member. [SM 86]
- Directors are appointed by the company **in general meeting**, unless the articles provide another method. [SM 86]
- No appointment without a **DIN**. The person gives his DIN and a declaration that he is **not disqualified**, and files his **consent** with the Registrar within **30 days** in **DIR-12**. Consent filing does not apply to Government appointees or section 8 companies. [SM 86]

**ROTATION s.152(6)**

- At least **two-thirds** of directors retire by rotation (articles may make it more, or all). Directors appointed by CG, BIFR or FIs/banks are not counted. [SM 86]
- At every AGM **one-third** of the rotational directors retire (nearest to one-third). The **longest in office** since their last appointment go first; if they were appointed the same day, by agreement or **by lot**. [SM 86]
- The retiring director's re-appointment is placed before the meeting by default, unless he is disqualified. [SM 87]

**VACANCY NOT FILLED s.152(7)**

- The meeting stands **adjourned to the same day next week**, same time and place (the next working day if that is a national holiday). [SM 87]
- If it is not filled there either, the retiring director is **deemed re-appointed**, unless: his re-appointment was put and **lost**; he said in writing he is **unwilling**; he is **disqualified**; a special or ordinary resolution is needed by the Act; or **s.162** applies. [SM 87]
- s.152(6)–(7) do not apply to a **100% Government company** or its wholly-owned subsidiary. [SM 87]

### s.160: a person other than a retiring director stands for election [SM 87–88]

**NOTICE** the candidate or a member leaves a written notice at the registered office at least **14 days** before the meeting [SM 87] → **DEPOSIT** **₹1,00,000**, refunded if he is elected or gets **more than 25%** of valid votes. No deposit if NRC or Board recommends him [SM 87] → **COMPANY INFORMS MEMBERS** at least **7 days** before the meeting (Rule 13): individual notices (e-mail or in writing) + its website [SM 87–88] → **OR ADVERTISES** at least **7 days** before, once in a **vernacular** newspaper of the district **AND** once in an **English** newspaper circulating there [SM 88]

**s.160 does not apply to:** a Government company whose **entire** paid-up capital is held by Government(s) · its wholly-owned subsidiary · a **private company** · a company whose **articles provide for election by ballot**. [SM 88]

**EXAM ANGLE: ASKED IN DEC'25 Q2(a) AND JUN'26 Q3(a), AND IN ICMAI'S MQP. THE THREE SITUATIONS AND THEIR ANSWERS**

| Situation | Answer |
|---|---|
| (i) the company is a **Government company** and the Government was told | s.160 **does not apply** to a Government company whose entire paid-up capital is held by Government, so the member has no right to propose under s.160; the deposit procedure does not arise. (If Government holds less than 100%, s.160 applies normally.) |
| (ii) the **articles provide for election by ballot** | s.160 **does not apply**; directors are elected by ballot as the articles say, so the proposal is not valid under s.160. |
| (iii) public company, no individual notices, advertised **only in a vernacular newspaper** 7 days before | **Not valid.** Rule 13 lets the company skip individual notices only if it advertises at least 7 days before in a vernacular newspaper **and** in an English newspaper circulating in the district. The member's own notice (14 days before, with ₹1 lakh) is in order. |

### Proportional representation, s.163 [SM 90–91]

The articles may provide for at least **two-thirds** of directors to be appointed by proportional representation (single transferable vote, cumulative voting or similar), once every **3 years**. It gives the minority fair representation. Casual vacancies are filled under s.161(4). It does not apply to 100% Government companies or their wholly-owned subsidiaries. [SM 90–91]

## 3 Additional, alternate, nominee and casual-vacancy directors (s.161); small shareholders' director (s.151)

| Type | Who appoints · when · how long | Traps |
|---|---|---|
| **Additional** 161(1) | the **Board**, if the **articles** allow, at any time. Holds office **up to the next AGM** or the last date the AGM should have been held, **whichever is earlier** [SM 88] | a person who **failed to be appointed at a general meeting cannot be made an additional director** (Jun'24 Q4(b)) [SM 88] |
| **Alternate** 161(2) | the **Board**, if authorised by the articles or a general-meeting resolution, in place of a director absent from India for **at least 3 months** [SM 88] | not someone already an alternate in the company · for an ID, must qualify as an ID · vacates when the original **returns to India** · term no longer than the original's · whether to appoint is the **Board's** choice, not the original director's [SM 88–89] |
| **Nominee** 161(3) | the **Board**, subject to the articles, appoints the person nominated by an institution (under a law or an agreement) or by Government through its shareholding [SM 89] | "nomination" is not "appointment": the Board must still appoint properly · a nominee **cannot be an ID** (s.149(6)) [SM 84] [SM 89] |
| **Casual vacancy** 161(4) | a director appointed in general meeting leaves before his term ends → the **Board** fills it at a Board meeting, **approved at the next general meeting** [SM 89] | the new director holds office only until the date the vacating director would have held it [SM 89] |

**SM example:** the retired CMD of a Government steel plant is appointed the next day as a full-time additional director of a private steel company; he holds office till the next AGM. [SM 88]

**SMALL SHAREHOLDERS' DIRECTOR (s.151): LISTED COMPANIES**

- **Small shareholder** = holds shares of nominal value **up to ₹20,000** [SM 89]
- Elected on notice from **1,000** small shareholders or **one-tenth** of them, **whichever is lower**; the company may also appoint one **suo motu** [SM 89–90]
- Notice of the candidate at least **14 days** before the meeting, with his DIN, a "not disqualified" statement and his consent [SM 90]
- Treated as an **ID** if he qualifies under s.149(6) [SM 90]

**ITS LIMITS**

- **not** liable to retire by rotation; tenure at most **3 consecutive years**; **no re-appointment** [SM 90]
- small shareholders' director in at most **2 companies**, and the second must not compete with the first [SM 90]
- for **3 years** after leaving, not associated with the company in any other capacity [SM 90]
- vacates on a s.164 disqualification, a s.167 vacancy, or losing independence [SM 90]

**MEMORY HOOK: s.161 IN ONE LINE**

**A-A-N-C**: **A**dditional till the AGM · **A**lternate while abroad 3 months · **N**ominee because someone nominated · **C**asual for the rest of the term. The Board appoints all four.

## 4 Disqualification, vacation, resignation and removal

**s.164(1): NOT ELIGIBLE FOR APPOINTMENT IF HE ...**

a. is of **unsound mind**, so declared by a court
b. is an **undischarged insolvent**
c. has **applied to be declared insolvent**, application pending
d. was **convicted** and sentenced to at least **6 months**, and **5 years** have not passed since the sentence ended. With a sentence of **7 years** or more: never, in any company
e. is under a court or Tribunal **disqualification order**
f. has **not paid calls** on his shares for **6 months** after the last date
g. was convicted under **s.188** (RPTs) in the last **5 years**
h. has **no DIN**
i. holds more directorships than **s.165(1)** allows

[SM 91]

**s.164(2): THE DEFAULTING-COMPANY RULE**

A director of a company that (a) has not filed financial statements or annual returns for **3 continuous financial years**, or (b) has not repaid deposits or debentures, interest, or preference dividend for **1 year or more** cannot be re-appointed there or appointed elsewhere for **5 years**. A new appointee in a defaulting company gets **6 months'** grace. Not applicable to **Government companies**. A private company's articles may add more disqualifications. [SM 91–92]

**When (d), (e), (g) take effect:** not for **30 days** from the conviction or order; if an appeal is filed within 30 days, until **7 days** after it is disposed of; if a further appeal is filed within 7 days, until that is disposed of. [SM 92]

### s.167: the office becomes vacant if he ... [SM 93–94]

1. incurs a **s.164 disqualification**. Under s.164(2) he vacates in **all companies except the defaulting one**
2. **absents himself from all Board meetings for 12 months**, with or without leave
3. acts against **s.184** (contracts in which he is interested)
4. **fails to disclose** his interest under s.184
5. is **disqualified** by a court or Tribunal order
6. is **convicted** and sentenced to at least **6 months** (with the same 30-day and 7-day appeal relief)
7. is **removed** under the Act
8. was a director because of his **job in the holding, subsidiary or associate company**, and that job ends

If he acts as a director knowing the office is vacant: fine **₹1 lakh to ₹5 lakh**. If **all** directors vacate, the **promoter** (or else the Central Government) appoints directors until the general meeting does. A private company's articles may add grounds. [SM 94]

**RESIGNATION s.168 (ICMAI PTP Q2(b))**

1. the director gives **written notice** to the company
2. the **Board takes note** of it
3. the company files **DIR-12** with the Registrar within **30 days** and posts it on its **website**
4. it is mentioned in the **directors' report** at the next general meeting
5. the director **may** send a copy with detailed reasons to the Registrar within **30 days** in **DIR-11**

[SM 92]

**REMOVAL s.169 (Dec'24 MCQ: ordinary resolution)**

1. by **ordinary resolution**, after giving him a **reasonable opportunity of being heard**. Not for a director appointed by the **Tribunal (s.242)**. An ID in his **second term** can be removed only by **special resolution**. Directors elected by proportional representation (s.163) cannot be removed this way
2. **special notice** from members to remove him or to appoint someone in his place
3. the company sends him a copy at once; he may be **heard at the meeting** (member or not)
4. the vacancy may be filled at the **same meeting** if special notice was given; the new director serves the **remaining term**. Otherwise it is filled as a casual vacancy, but the **removed director cannot be re-appointed**
5. his right to **compensation or damages** stays

[SM 92–93]

## 5 Managing director, whole-time director, manager (s.196) and KMP (s.203)

| Term | Meaning |
|---|---|
| **Managing director** 2(54) | a director entrusted with **substantial powers of management** by the articles, an agreement, or a general-meeting or Board resolution. Routine acts (affixing the seal, signing cheques or negotiable instruments, share certificates, registering transfers) are **not** "substantial powers" [SM 94] |
| **Whole-time director** 2(94) | a director in the **whole-time employment** of the company, e.g. Director (Finance) or Director (Commercial): an executive director [SM 94] |
| **Manager** 2(53) | an individual who, under the Board's control, manages the **whole or substantially the whole** of the affairs [SM 94–95] |

**s.196: APPOINTING MD / WTD / MANAGER**

- never an MD **and** a manager at the same time [SM 95]
- term at most **5 years** at a time; re-appointment not earlier than **1 year** before the term ends [SM 95]
- **not** if: below **21** or has reached **70** (70+ allowed by **special resolution**); an undischarged or adjudged insolvent; has suspended payments to creditors; convicted and sentenced to more than **6 months** [SM 95]
- **Schedule V:** not jailed, or fined above **₹1,000**, under the **16** listed Acts; not detained under COFEPOSA; **resident in India**, i.e. stayed **12 months** continuously before appointment [SM 95]

**PROCEDURE s.196(4)**

1. the **Board** approves the appointment, terms and remuneration at a meeting
2. approval by **shareholders' resolution** at the next general meeting
3. if it departs from **Schedule V**: **Central Government** approval
4. the notice states the terms, remuneration and directors' interest
5. return in **MR-1** to the Registrar within **60 days**

**s.196(5):** if the general meeting does not approve, his acts **before** that are **deemed valid**. [SM 95–96]

**⚠ SM SAYS TWO THINGS · AND A PAST QUESTION THE SM DOES NOT COVER**

The SM's Schedule V list ends with "any act done by him deemed to be **invalid**", but s.196(5) on the next page says acts before non-approval are deemed **valid**. **Write "valid" (s.196(5)).** [SM 95–96]
**Dec'23 Q5(a)** "How far will the acts of a director be invalid if his appointment is not valid?" is answered by **s.176**, which is not in the SM. Acts done by a person as a director are **not invalid** just because a defect or disqualification in his appointment, or its termination, is noticed later. But this gives **no validity to acts done after** the company has noticed the defect.

### s.203: Key Managerial Personnel [SM 96–97]

**WHO AND WHEN**

- **Listed** companies and **public** companies with paid-up capital ≥ **₹10 crore** must have whole-time KMP: (1) **MD or CEO or manager** (if none, a WTD); (2) **CS**; (3) **CFO** [SM 96]
- One person may **not** be both **chairperson** and **MD/CEO**, unless the **articles allow** or the company does not carry on **multiple businesses** [SM 96]
- Appointed by **Board resolution** stating terms and remuneration [SM 96]
- A KMP vacancy is filled by the Board within **6 months** [SM 97]

**MORE THAN ONE COMPANY (JUN'26 Q2(b))**

- A whole-time KMP shall **not hold office in more than one company** at the same time, **except in its subsidiary** [SM 96]
- He may be a **director** of any company **with the Board's permission** [SM 96]
- A company may appoint as its MD a person who is MD or manager of **one, and not more than one,** other company, by a **unanimous Board resolution** of the directors present, with **specific notice** to all directors in India [SM 97]
- *Example:* X is CFO of A Ltd. He can also be CFO of A's subsidiary B Ltd, and a director of C Ltd with A's Board permission, but not CFO of unrelated D Ltd.

## 6 Managerial remuneration (s.197–s.202)

| Who (public companies) | Limit: % of net profits | To pay more |
|---|---|---|
| **All directors** incl. MD, WTD, manager, together | **11%** | general meeting, subject to Schedule V |
| **One** MD / WTD / manager | **5%** | special resolution |
| **More than one** MD / WTD / manager, together | **10%** | special resolution |
| Other directors, **when there is** an MD or WTD | **1%** | special resolution |
| Other directors, **when there is no** MD or WTD | **3%** | special resolution |

If the company has defaulted to a bank, PFI, NCD holders or a secured creditor, their **prior approval** comes before the special resolution. The **auditor certifies** that the remuneration is within limits. Net profit is computed under **s.198**, **without deducting the**

**directors' remuneration**. [SM 97]

- **Fixed by** the articles, a resolution, or a special resolution if the articles require. It **includes** pay for any other capacity, except **professional services** where the NRC or Board finds he is qualified for that profession. [SM 98]
- **Sitting fees:** up to **₹1 lakh per meeting** of the Board or a committee. For IDs and women directors, not less than other directors get. Sitting fees are **outside** the % limits. [SM 98]
- **Mode:** monthly payment, a % of net profits, or both. Fidelity or misfeasance insurance premium is **not** remuneration. [SM 98]
- **No or inadequate profits:** pay only under **Schedule V**, otherwise with **Central Government** approval. No increase is effective unless it meets Schedule V. [SM 98–99]
- **Excess drawn:** refund within **2 years** (held in trust until then). Waiver only by **special resolution** within 2 years. [SM 99]
- **Listed company's Board report:** each director's pay as a **ratio to the median employee**; the **top 10** earners; anyone paid at least **₹1.25 crore** a year or **₹8.5 lakh a month** (SM: "eight lakh fifty thousand"), or more than the MD while holding **2%**+ equity with spouse and children. [SM 99]
- An MD or WTD on commission may also take pay or commission from the **holding or subsidiary company**, if disclosed in the Board's report. [SM 99]
- **Contravention:** fine **₹1 lakh to ₹5 lakh**. The **auditor's report** states whether the remuneration complies. [SM 100]
- **s.200:** when fixing pay with no or inadequate profits, the Government or company considers the financial position, pay from other capacities and companies, qualifications, performance in the **3 preceding years**, the pay-to-performance link, proportionality, and the director's securities and pledges. [SM 102]

**⚠ SM SAYS TWO THINGS**

On waiving a refund, the SM gives both "by **special resolution** within two years" (the current Act) and "unless permitted by the **Central Government**" (the old Act). **Write special resolution.** [SM 99]

**s.198 NET PROFIT IN BRIEF**

**Add:** Government bounties and subsidies. **Do not credit:** premium on shares or debentures, profit on forfeited shares, capital profits, profit on sale of fixed assets (except the part up to original cost), fair-value and revaluation gains. **Deduct:** working charges, directors' remuneration, staff bonus and commission, interest, repairs (not capital), depreciation under s.123, past losses, legal damages, bad debts. **Do not deduct:** income tax, voluntary compensation, capital losses, fair-value changes. [SM 100–101]

**s.202: COMPENSATION FOR LOSS OF OFFICE**

Payable **only to an MD, WTD or manager**. **Not** payable if he resigns on a reconstruction or amalgamation and is re-employed; resigns in the normal course; vacates under s.167(1); the winding up was due to his negligence; he committed fraud, breach of trust or gross mismanagement; or he brought about his own termination. **Cap:** his pay for the rest of the term or **3 years**, whichever is **shorter**, on his average pay over the last 3 years. Nothing is paid if winding up starts within **12 months** after he leaves and the assets cannot repay shareholders' capital. [SM 108–109]

**Recovery on restatement:** if the financial statements are restated for fraud or non-compliance, any excess pay (including stock options) is recovered from past or present MDs, WTDs, managers or CEOs. [SM 109]

## 7 Powers of the Board (s.179) and restrictions (s.180)

The Board may exercise **all powers the company has**, collectively. No individual director has any power unless specifically authorised. The articles and the general meeting may restrict it, but a later restriction does **not invalidate a prior valid act** of the Board. [SM 102]

**ONLY BY RESOLUTION AT A BOARD MEETING, s.179(3) + Rule 8**

1. make **calls** on unpaid shares
2. authorise **buy-back** (s.68)
3. **issue securities**, including debentures
4. **borrow** money
5. **invest** the company's funds
6. grant **loans**, guarantees or security
7. approve the **financial statements and Board's report**
8. **diversify** the business
9. approve **amalgamation, merger, reconstruction**
10. **take over** a company or acquire a controlling stake
11. Rule 8: **political contributions** · appoint or remove **KMP** · appoint **internal and secretarial auditors**

The Board may **delegate** borrowing, investing and lending to a committee, the MD, the manager or principal officer, or a branch's principal officer. [SM 102–103]

**ONLY WITH SHAREHOLDERS' SPECIAL RESOLUTION, s.180(1) (DEC'23 Q3(a))**

a. **sell, lease or dispose** of the whole or substantially the whole of an **undertaking**. Undertaking = investment above **20%** of net worth, or **20%** of total income. Substantially the whole = **20%** or more of its value
b. **invest** merger or amalgamation **compensation** other than in trust securities
c. **borrow** beyond **paid-up capital + free reserves + securities premium**. Temporary loans from bankers are excluded (repayable on demand or within **6 months**, not for capital purposes); so are bank deposits taken by a banking company. The resolution states the **maximum amount**
d. **remit** or give time to repay a **debt due from a director**

A buyer or lessee in **good faith** is protected, as are sales in the ordinary course of a company whose business is selling or leasing. The SM says s.180 does not apply to a **private company**. [SM 103–104]

**Shareholders may step in** when the directors act mala fide, the Board is incompetent (e.g. all directors interested, or no valid Board), or there is a deadlock. [SM 104]

## 8 Director Identification Number (DIN), s.153–159

**APPLY (s.153, RULE 9)**
**DIR-3** online with photo, ID and address proof, signature; verified by the company's CS, MD, director, CEO or CFO. At incorporation via **SPICe INC-32** for up to **3** directors [SM 105]

→

**ALLOT (s.154, RULE 10)**
Central Government decides within **1 month**; defects cured within **15 days**; DIN valid **for life** [SM 105–106]

→

**DIRECTOR → COMPANY (s.156)**
within **1 month** of receiving the DIN (DIR-3B) [SM 106–107]

→

**COMPANY → ROC (s.157)**
within **15 days** (DIR-3C). Default: fine **₹25,000 to ₹1,00,000** on the company and each officer [SM 106–107]

- **Only one DIN** per person (s.155). Mention the DIN in every return (s.158). [SM 106–107]
- **s.159 penalty** for breaking s.152, 155 or 156: up to **₹50,000**, plus **₹500** a day if it continues. [SM 107]
- **Cancelled or deactivated** if: duplicate · obtained wrongfully · death · unsound mind · insolvency · surrendered in **DIR-5** (never used). [SM 107]
- **Change of particulars: DIR-6** within **30 days**, certified by a practising CA, CS or CMA; tell the companies within **15 days**. [SM 107–108]
- **Dec'24 MCQ:** the DIN application procedure is in **Rule 9**. [SM 105]

**DEC'26 SUPPLEMENTARY: DIRECTOR KYC (COMPANIES (APPOINTMENT AND QUALIFICATION OF DIRECTORS) AMENDMENT RULES, 2025) · EFFECTIVE 31 MARCH 2026**

- Annual KYC is replaced by an abridged KYC **once in every 3 consecutive financial years**: **DIR-3 KYC** web filing by **30 June** after every third year. [Supp Dec'26 p.2]
- A change in mobile number, e-mail or residential address is updated within **30 days** of the change. [Supp Dec'26 p.2]

# 9 Loans to directors (s.185), disclosure of interest (s.184), related party transactions (s.188)

### s.185: LOANS TO DIRECTORS

- **Prohibited:** a loan, guarantee or security for a director of the company or its holding company, a partner or relative of such a director, or a firm in which such a director or relative is a partner. [SM 109]
- **Allowed to "a person in whom a director is interested"** (a private company where he is director or member; a body corporate where directors control **25%**+ of votes; a body corporate whose board follows his directions) if (a) a **special resolution** is passed with full particulars, and (b) the money is used for its **principal business**. [SM 109]
- **Exempt:** a loan to an MD/WTD under conditions of service for all employees, or a scheme approved by special resolution · a lending company charging at least the **G-sec yield** (1, 3, 5 or 10 years, nearest the tenor) · a holding company's loan to, or guarantee for, its **wholly-owned subsidiary** · a guarantee for a bank loan to a subsidiary (used for principal business). [SM 109–110]
- **Penalty:** company **₹5 lakh to ₹25 lakh**; director and borrower: up to **6 months** in jail, or a fine of ₹5–25 lakh, or both. [SM 110]
- **Private company exemption** if: no body corporate has invested in it; borrowings below **twice** its paid-up capital or **₹50 crore**, whichever is lower; no default. [SM 110]

### s.184: DISCLOSURE OF INTEREST

- **When:** at the **first Board meeting** he attends, at the first meeting **each financial year**, and at the first meeting **after any change**, by written notice. [SM 111]
- **Contracts:** if he (alone or with another director) holds more than **2%** of the other body corporate, or is its promoter, manager or CEO, or is a partner, owner or member of the firm: he **discloses and does not participate**. [SM 111]
- **Result:** the contract is **voidable at the company's option**; penalty **₹1 lakh**. **Exception:** contracts between two companies where directors hold **2% or less**. [SM 111]
- **Cases:** a formal disclosure is not needed if the whole Board knows (*Ramakrishna Rao v. Bangalore Race Club*), but *Guinness v. Saunders* requires formal disclosure even when it is known. "Interest" includes family closeness (*Firestone Tyre v. Synthetics & Chemicals*). [SM 111–115]
- **Quorum:** if interested directors are **two-thirds or more** of the Board, the quorum is the non-interested directors present, at least **2** (s.174). [SM 114]

## s.188: related party transactions (RPTs) [SM 112–114]

### NEED BOARD CONSENT AT A MEETING

a. sale, purchase or supply of goods or materials
b. selling, disposing of or buying property
c. leasing property
d. availing or rendering services
e. appointing an agent for buying or selling
f. a related party's appointment to an **office or place of profit**
g. underwriting the company's securities

The related party **shall not vote** (except where **90%** of shareholders are related parties). **No shareholder approval** is needed for ordinary-course, arm's-length deals or holding–WOS deals. Unratified contracts are voidable. [SM 112]

### ALSO NEED SHAREHOLDERS' RESOLUTION ABOVE ...

| | |
|---|---|
| goods (sale, purchase, supply) | **10%** of turnover or **₹100 cr**, lower |
| property (buy, sell) | **10%** of net worth or **₹100 cr**, lower |
| leasing | **10%** of net worth or turnover, or **₹100 cr** |
| services | **10%** of turnover or **₹50 cr**, lower |
| office or place of profit | pay above **₹2.5 lakh a month** |
| underwriting | above **1%** of net worth |

The limits apply per transaction or together during a financial year. [SM 113–114]

**OMNIBUS APPROVAL, RULE 8A (DEC'23 Q2(b), 7 MARKS: THE SM'S OWN SENTENCE)**

**SM WORDS** "All related party transactions shall require approval of the Audit Committee and the Audit Committee may make omnibus approval for related party transactions proposed to be entered into by the company subject to the following conditions":

1. The Audit Committee, **after Board approval**, specifies the criteria: maximum value a year and per transaction; extent of disclosures; periodic review; transactions not allowed under omnibus approval.
2. It considers the **repetitiveness** of the transactions and the **justification** for omnibus approval.
3. It satisfies itself that the approval is **needed** and in the **company's interest**.
4. The approval states the **related parties**, the nature and duration, the **maximum amount**, and the indicative or current price and variation formula. For unforeseen needs: up to **₹1 crore per transaction**.
5. It is valid for at most **one financial year**.
6. Never for **selling or disposing of the undertaking**.
7. Any other conditions the Audit Committee thinks fit.

[SM 112–113]

## 10 Model answers: our top two Dec'26 questions on 1.5

**MODEL ANSWER 1 · BOARD COMPOSITION CASE (DEC'24 Q3(a), JUN'25 Q1) · 7 MARKS**

**Facts (Dec'24):** Mirinda Ltd, an unlisted public company with paid-up capital ₹40 crore and turnover ₹350 crore. Board: the promoter MD; a non-executive Chairman (not an ID); Director (Finance); Director (Operations), related to the promoter. CS: Ms Supriti. A nationalised bank will nominate a director (a woman, in Jun'25). Is the Board properly constituted, and what must be done?

| Point | Provision | Applied to the facts |
|---|---|---|
| Number | public company: at least 3 directors (s.149(1)) [SM 83] | 4 directors: **complies** |
| Independent directors | unlisted public company with paid-up capital ≥ ₹10 crore or turnover ≥ ₹100 crore: **at least 2 IDs** (s.149(4), Rule 4) [SM 84] | ₹40 cr capital and ₹350 cr turnover, so 2 IDs are needed. **None qualifies:** the MD and the two functional directors are whole-time; Director (Operations) is **related to the promoter**; the Chairman is not an ID. → **Appoint 2 IDs** |
| Woman director | public company with turnover ≥ ₹300 crore: at least **1 woman director** (Rule 3) [SM 83–84] | turnover ₹350 cr, so one is needed; there is none → **appoint one** |
| Bank's nominee | the Board appoints a nominee under s.161(3); a nominee **cannot be an ID** (s.149(6)) [SM 84–89] | she can sit as nominee director. She **does not count as an ID**, but the rule asks only for "a woman director", so she can meet the woman-director requirement (Jun'25 Q1(iv), option C) ⚠ |
| KMP | public company with paid-up capital ≥ ₹10 crore: MD/CEO + CS + **CFO** (s.203, Rule 8) [SM 96] | MD and CS exist; **designate or appoint a CFO** if Director (Finance) is not formally the CFO |

**Conclusion:** the Board is **not properly constituted**. Mirinda must appoint **two independent directors** and **a woman director** (the bank's woman nominee can fill that), and make sure a **CFO** is in place.

⚠ ICMAI's suggested answer is not with us yet. The nominee-as-woman-director point follows the rule's wording; check it when the suggested answers are downloaded.

**MODEL ANSWER 2 · MANAGERIAL REMUNERATION CASE (JUN'23 Q2(b), 8 MARKS · OVERDUE)**

**Facts:** AB Ltd, a listed company managed by an MD. Proposal: (i) MD, Mr M: commission at **5%** of net profits. (ii) Other directors: **₹50,000 a month** each plus commission at **1%** of net profits, with all their pay together capped at **2%** of net profits. Examine.

1. **Provision.** s.197(1): total pay to all directors ≤ **11%** of net profits; one MD ≤ **5%**; other directors ≤ **1%** where there is an MD. Exceeding a limit needs a **special resolution**. Net profit is computed under s.198 without deducting directors' pay. Pay may be monthly, a % of profits, or both (s.197(6)). Sitting fees are outside the limits. [SM 97–98]
2. **MD's 5% commission:** exactly at the 5% limit for one MD, so it is **valid** without a special resolution (shareholders still approve his terms under s.196).
3. **Other directors:** their monthly pay plus commission may reach **2%**, above their **1%** limit, so this part needs a **special resolution** in general meeting. Monthly payment is a permitted mode.
4. **Overall:** 5% + up to 2% = up to 7%, **within 11%**.
5. **Conclusion:** the MD's commission is in order. The other directors' package is valid only if the shareholders pass a **special resolution**. The auditor must state in his report that the remuneration complies with s.197.

## SM exercise MCQs on 1.5, with answers **(SM 164–171 = ICMAI MCQ bank Q39–83; ★ = asked in an exam)**

| | | | |
|---|---|---|---|
| 39 additional director's tenure up to | **next AGM** | 48 s.203 provides for appointment of | **KMP** |
| 40 alternate: original absent from India at least | **3 months** | 49 MD eligibility and conditions are in Schedule | **V** |
| 41 woman director required if | **listed, or ₹300 cr turnover (either)** | 50 maximum pay to all managerial personnel | **11%** |
| 43 WTD appointed for a term of | **5 years** | 51 IDs are not entitled to | **stock options** |
| 44 deposit with s.160 proposal | **₹1 lakh** | 52 Board's report is addressed to | **members** |
| 45 small shareholder: face value up to ★ | **₹20,000** | 53 Board's powers may be restricted by | **Act, articles, GM: any or all** |
| 46 remove a director by ★ | **ordinary resolution** | 54 RPTs are in section | **188** |
| 47 MD's appointment ratified in AGM by | **ordinary resolution** | 56 IDs meet separately, a year | **once** |
| 64 executive chairman: IDs at least | **half** | 80 a CFO must be a | **none (no fixed qualification)** |
| 81 sitting fee: Board vs committee | **may differ** | 82 disclosure of interest is | **all or any (first meeting, yearly, on change)** |
| 83 Board quorum | **⅓ or 2, higher** | MCQ bank 266: small sh. director in at most | **2 companies** |

Not in the 1.5 SM text, but in the MCQ bank: Q51 (IDs get no stock options) and Q64 (half IDs with an executive chairman) come from the SEBI/governance rules in Module 3.

## R Revision: every number in 1.5

| Rule | Number |
|---|---|
| directors: public / private / OPC | 3 / 2 / 1 |
| maximum directors (more by special resolution) | 15 |
| woman director: paid-up / turnover (public) | ₹100 cr / ₹300 cr |
| woman director in a new company within | 6 months |
| ID or woman vacancy: next Board meeting or | 3 months, later |
| resident director stay | 182 days |
| IDs in a listed company | one-third |
| 2 IDs if paid-up / turnover / borrowings | ₹10 cr / ₹100 cr / > ₹50 cr |
| ID: pecuniary limit / look-back | 10% income / 2 yrs |
| ID: relative's holding limit | ₹50 lakh or 2% |
| ID: KMP/employee cooling-off | 3 yrs |
| ID: voting power / NGO receipts | 2% / 25% |
| ID databank test exemption | 10 yrs experience |
| consent DIR-12 filed within | 30 days |
| rotational / retire each AGM | ⅔ / ⅓ |
| s.160 notice / deposit / refund if votes > | 14 days / ₹1 lakh / 25% |
| company informs or advertises members | 7 days before |
| alternate: director abroad at least | 3 months |
| small shareholder nominal value | ≤ ₹20,000 |
| small shareholders' notice: 1,000 or | 1/10, lower |
| small sh. director: tenure / companies / cooling | 3 yrs / 2 / 3 yrs |
| proportional representation: share / every | ⅔ / 3 yrs |
| s.164: sentence / wait / bar for life | 6 m / 5 yrs / 7 yrs |
| unpaid calls for | 6 months |
| s.164(2): not filed / deposit default / bar | 3 FYs / 1 yr / 5 yrs |
| grace for new appointee in defaulter | 6 months |
| appeal relief | 30 days / 7 days |
| absent from all Board meetings for | 12 months |
| acting while vacated: fine | ₹1–5 lakh |
| resignation DIR-12 / DIR-11 | 30 / 30 days |

| Rule | Number |
|---|---|
| MD/WTD term / re-appoint not before | 5 yrs / 1 yr |
| MD/WTD age (70+ by special resolution) | 21–70 |
| Schedule V: Acts / fine / residence | 16 / ₹1,000 / 12 months |
| MR-1 within | 60 days |
| KMP mandatory: paid-up (public) | ₹10 crore |
| KMP vacancy filled within | 6 months |
| overall / 1 MD / >1 MD | 11% / 5% / 10% |
| others with MD / without MD | 1% / 3% |
| sitting fee per meeting, maximum | ₹1 lakh |
| refund of excess pay within | 2 years |
| disclosure: yearly / monthly pay | ₹1.25 cr / ₹8.5 lakh |
| s.197 contravention fine | ₹1–5 lakh |
| s.202 cap / winding-up window | 3 yrs / 12 months |
| s.180 undertaking / substantially whole | 20% / 20% |
| temporary loans repayable within | 6 months |
| DIN: CG decides / defects / SPICe directors | 1 month / 15 days / 3 |
| DIN to company / company to ROC | 1 month / 15 days |
| s.157 fine | ₹25,000–₹1 lakh |
| s.159 penalty | ₹50,000 + ₹500/day |
| DIR-6 change / tell companies | 30 / 15 days |
| KYC (Dec'26 supp.): every / by | 3 FYs / 30 June |
| s.185: controlled body corporate | 25% votes |
| s.185 penalty: company / jail | ₹5–25 lakh / 6 months |
| s.185 private-co exemption: borrowings < | 2× capital or ₹50 cr |
| s.184 shareholding test / penalty | 2% / ₹1 lakh |
| interested ≥ ⅔ → quorum at least | 2 |
| RPT: goods / property | 10% or ₹100 cr |
| RPT: services / office of profit | ₹50 cr / ₹2.5 lakh pm |
| RPT: underwriting / related holders | 1% NW / 90% |
| omnibus: unforeseen / validity | ₹1 cr / 1 FY |

# 1.4 · Accounts and Audit

P13 · Module 1 · Companies Act, 2013 · s.128–148 + CARO 2020

SM pp. 51–81 (31 pages). **The second-highest topic in P13:** 64 marks in 7 papers, asked in 6 of them, with two halves in Jun'26.

| Paper | What was asked | Marks |
|---|---|---|
| Jun'23 | MCQ: who may inspect the books (any director) · Q8(a) **auditor case**: (i) can he be removed, and how? (ii) what if he resigns? (iii) a qualified report | 2 + 10 |
| Dec'23 | MCQ: copies of FS at shorter notice (95%) · Q1 (xii)–(xv) **4-MCQ case** on authenticating the FS and the Board's report | 2 + 8 |
| Dec'24 | Q2(b) books of account in **electronic form** (s.128) | 7 |
| Jun'25 | MCQ: internal auditor criteria for a private company | 2 |
| Dec'25 | Q1 (i)–(iv) **4-MCQ auditor case** (resignation without ADT-3, debt ₹2 lakh, charged with fraud, fees) · Q5(a) **fraud reporting**, s.143(12) | 8 + 7 |
| Jun'26 | MCQs: statutory auditor = practising CA; Board's report signed by · Q3(b) **first and subsequent auditors, tenure, rotation, disqualifications** · Q5(a) **Board's report: contents, authentication, filing** | 4 + 7 + 7 |

**HOW IT IS EXAMINED**

- **The auditor is the favourite:** appointment, rotation, removal or resignation, eligibility. It was asked 8 times, and ICMAI's MQP repeated the Dec'25 auditor MCQ case.
- **Board's report and authentication** (s.134): 6 times. **Books of account** (s.128) and **fraud reporting** (s.143(12)): once each as a 7-marker.
- **Never asked yet:** CARO 2020 and s.144 prohibited services. The ICMAI postal paper had "independence of the auditor" as an 8-marker.

**DEC'26: OUR PREDICTION (A PREDICTION, NOT A PROMISE)**

Tier **A**. Expected **9–16 marks**: a 7-mark theory or case question plus 2–4 MCQs, often a 4-MCQ case set. Likely questions:

1. Auditor wants to resign / company wants to remove him: procedure and filings (s.140, ADT-3)
2. Services an auditor cannot render (s.144) and his independence
3. Fraud reporting (s.143(12)), now only by e-form ADT-4 (Jun'26 supplementary)
4. Books of account (s.128) and internal audit (s.138)

**MAP OF THIS PACK (★ = exam weight)**

1. Books of account s.128 ★★
2. Financial statements s.129, 133 ★
3. Authentication + Board's report s.134 ★★★
4. Copies to members s.136, filing s.137 ★★
5. Internal audit s.138 ★
6. Appointing the auditor s.139 ★★★
7. Removal, resignation s.140 ★★★
8. Eligibility s.141, fees s.142 ★★
9. Powers, duties, fraud reporting s.143 ★★
10. s.144–148: services, signing, penalties, cost audit ★
11. CARO 2020 ★ · CSR pointer
12. Model answers · MCQ case set · numbers · SM MCQs

## 1 Books of account (s.128) · Dec'24 Q2(b)

**WHAT IT IS** Every company keeps **books of account**: records of money received and spent, sales and purchases, assets and liabilities, and cost items where s.148 applies. They are kept on an **accrual basis** and by **double entry**, and must give a **true and fair view**, branches included. [SM 51]

### WHERE · WHO · HOW LONG

- At the **registered office**. The Board may choose another place **in India**, with a notice to the ROC giving the full address within **7 days** of the Board's decision. [SM 51]
- **Branch** (in India or abroad): the branch may keep its own books, but sends **summarised returns** periodically to the registered office. [SM 52]
- **Inspection:** by **any director**, during business hours. For records kept abroad, summarised returns come to the RO **quarterly**; other information is given within **15 days** of the director's written request, and he must ask **himself**, not through an agent. A subsidiary's books are inspected only by a person authorised by Board resolution. [SM 52–53]
- **Preserve:** for at least **8 financial years** before the current year, with vouchers (all years if the company is younger). Longer if the CG so directs during an investigation. [SM 53]
- **Responsible:** the MD, the WTD in charge of finance, the CFO, or another person charged by the Board. Fine **₹50,000 to ₹5 lakh**. [SM 53]

### ELECTRONIC FORM (Rule 3): THE 7-MARK ANSWER

1. remain **accessible in India** for later reference
2. kept in the **original format** (or one that shows it accurately), **complete and unaltered**
3. information from branches is **not altered** and shows what the branch sent
4. can be **displayed in legible form**
5. a proper system for **storage, retrieval, display or printout**, as the Audit Committee or Board decides; not disposed of unless the law permits
6. **back-up kept on servers physically in India**, periodically, even if the books are kept abroad
7. every year, with the financial statements, the company tells the ROC the **service provider's name, IP address, location**, and the **cloud address** if kept on cloud

[SM 52]

**Financial year:** the year ending **31 March**. A company incorporated on or after **1 January** ends its first year on 31 March of the next year. The CG may allow a different year for a company with a foreign holding company or subsidiary. [SM 51]

## 2 Financial statements (s.129, 129A, 133)

### WHAT AND HOW

- **"Financial statement"** (s.2(40)): balance sheet · P&L (or income and expenditure account) · **cash flow statement** · statement of changes in equity · notes. An **OPC, small company or dormant company** may leave out the cash flow statement. [SM 53]
- They must give a **true and fair view**, follow the **accounting standards** (s.133), and use the **Schedule III** format. Insurance, banking and electricity companies use their own Acts' formats. [SM 54]
- The Board **lays them before every AGM**. [SM 54]
- **Deviation from AS:** disclose (a) the deviation, (b) the reasons, (c) the financial effect. [SM 55]
- **Contravention:** the MD, WTD (finance), CFO or person charged (else all directors): up to **1 year** in jail, or a fine of **₹50,000 to ₹5 lakh**, or both. [SM 55–56]

### CONSOLIDATED FS · s.129A · s.133

- A company with subsidiaries also prepares **consolidated FS** (an **associate counts** as a subsidiary here), lays them at the AGM, and attaches the subsidiaries' salient features in **AOC-1**. [SM 54]
- **Exempt from consolidating:** a wholly owned subsidiary (or a partly owned one whose other members, told in writing, do not object) that is **unlisted** and whose holding company files consolidated FS with the ROC. [SM 55]
- **s.129A** (2020): the CG may require periodic financial results, with Board approval and audit or limited review, filed within **30 days** of the period's close. [SM 56]
- **s.133:** the **CG prescribes the accounting standards** recommended by **ICAI**, after **NFRA** examines them. *SM MCQ 90: Central Govt.* [SM 56]

# 3 Authentication and the Board's report (s.134) · Jun'26 Q5(a), Dec'23 MCQ case

**AUTHENTICATION s.134(1), (2), (7)**

- The FS (consolidated too) are **approved by the Board** and then signed on its behalf by: the **chairperson**, if the Board authorises him, **or** two directors, one being the **MD**; the **CEO** if he is a director; the **CFO** wherever appointed; and the **CS** wherever appointed. [SM 56]
- **OPC:** signed by **one director**, for the auditor's report. [SM 56]
- The **auditor's report is attached** to every FS. A signed copy is issued with the **notes, the auditor's report and the Board's report**. [SM 56]

*Dec'23 case:* PQR has directors A–D, MD E and CS F; only directors B and C signed. That is **not valid**: with no authorised chairperson, the signatories must include the **MD (E)**, and the **CS (F)** must sign as he is appointed.

**SIGNING THE BOARD'S REPORT s.134(6) · SM MCQ 31 · Jun'26 MCQ**

Signed by the **chairperson if authorised by the Board**. Otherwise by at least **two directors, one of them the MD**, or by the director where there is only one. [SM 59]

**OPC:** the Board's report need only contain the Board's explanations on the auditor's qualifications. [SM 59]

**Contravention of s.134:** company **₹3 lakh**, each officer in default **₹50,000**. [SM 59]

## What the Board's report contains, s.134(3) + Rule 8 [SM 57–59]

a. **web address** of the annual return (s.92(3))
b. **number of Board meetings**
c. **Directors' Responsibility Statement**
d. **frauds reported by the auditor** under s.143(12), other than those reported to the CG
e. the **IDs' declaration** of independence (s.149(6))
f. **NRC policy** on directors' appointment and remuneration (not for Government companies)
g. Board's **explanation of every qualification** or adverse remark by the **auditor** and the **secretarial auditor**
h. loans, guarantees, investments under **s.186**
i. **RPTs** under s.188(1) in **AOC-2**
j. the **state of affairs**; amounts to **reserves**; recommended **dividend**
k. **material changes** between the year-end and the date of the report
l. **energy conservation, technology absorption, foreign exchange earnings and outgo**
m. **risk management policy** statement
n. **CSR policy** and initiatives, with the web address
o. **annual evaluation** of the Board, its committees and directors: listed companies, and public companies with paid-up capital ≥ **₹25 crore**
p. prepared on the **standalone FS**, with highlights of subsidiaries, associates and JVs

**JUN'26 SUPPLEMENTARY: COMPANIES (ACCOUNTS) SECOND AMENDMENT RULES, 2025 · EFFECTIVE 14 JULY 2025**

- The Board's report must also disclose the number of **sexual harassment (POSH) complaints** received, disposed of, and pending for more than **90 days**, plus a declaration of compliance with the **Maternity Benefit Act, 1961**. [Supp Jun'26 p.2]
- Filing moves fully to **MCA V3**: e-AOC-1, e-AOC-2 and a revised **AOC-4**. Signed FS, Board's report extracts and auditors' reports go in PDF/XBRL on the V3 portal only. [Supp Jun'26 p.2]

**DIRECTORS' RESPONSIBILITY STATEMENT, s.134(5) (SM MCQ 28: part of the Board's report)**

a. the applicable **accounting standards** were followed, with material departures explained
b. accounting policies were applied **consistently**, with reasonable and prudent judgments, for a **true and fair view**
c. proper care was taken to keep **adequate accounting records**, safeguard assets, and prevent and detect **fraud**
d. the accounts were prepared on a **going concern** basis
e. (listed companies) **internal financial controls** were laid down, adequate and operating effectively
f. **systems to ensure compliance with all laws** are adequate and operating effectively

[SM 59]

## 4 Copies to members (s.136) and filing with the Registrar (s.137)

**s.136: COPIES OF THE FINANCIAL STATEMENTS**

- Sent to every **member**, every **debenture trustee** and every other person entitled, at least **21 days** before the meeting, with the consolidated FS, auditor's report and annexures. [SM 60–61]
- **Shorter period** is valid if agreed by members who are a **majority in number** and hold at least **95%** of the voting paid-up capital (no share capital: 95% of voting power). *Dec'23 MCQ.* [SM 61]
- **Listed company:** complies by keeping the documents open for inspection at the RO for **21 days** and sending a statement of salient features (**AOC-3**). **Section 8 company:** 14 days instead of 21. [SM 61]
- Members inspect at the RO during business hours. **Electronic sending** is allowed for listed companies and public companies with net worth above **₹1 crore** and turnover above **₹10 crore**. A listed company puts its FS on its website, plus separate accounts of each subsidiary. [SM 61–62]
- **Penalty:** company **₹25,000**; each officer **₹5,000**. [SM 62]

**s.137: FILING WITH THE ROC (SM MCQ 33: 30 days of AGM)**

- **Adopted at the AGM:** file within **30 days** of the AGM. [SM 62]
- **Not adopted:** file the unadopted FS within **30 days** of the AGM; the ROC treats them as **provisional**. Once adopted at the adjourned AGM, file within **30 days** of it (late filing with additional fees is allowed up to **270 days** under s.403). [SM 62]
- **OPC:** within **180 days** of the year-end. [SM 63]
- Attach the accounts of **foreign subsidiaries** without a place of business in India. [SM 63]
- **AGM not held:** file the signed FS with a statement of reasons within **30 days** of the last date the AGM should have been held. [SM 63]
- **Penalty:** company **₹10,000** + **₹100 a day**, up to **₹2 lakh**. MD and CFO (else the director charged, else all directors): **₹10,000** + ₹100 a day, up to **₹50,000**. [SM 63]

## 5 Internal audit (s.138) · Jun'25 MCQ

| Company | Must appoint an internal auditor if, in the preceding financial year ... |
|---|---|
| **Listed** | always [SM 63] |
| **Unlisted public** | paid-up capital ≥ **₹50 crore** · OR turnover ≥ **₹200 crore** · OR bank/PFI loans above **₹100 crore** at any time · OR deposits ≥ **₹25 crore** at any time [SM 64] |
| **Private** | turnover ≥ **₹200 crore** · OR bank/PFI loans above **₹100 crore** at any time *(Jun'25 answer: "2 and 3")* [SM 64] |

**Who:** a **chartered accountant or cost accountant**, **in practice or not**, or another professional the Board decides. He may be an **employee**. It may be an individual, a firm or a body corporate. **Scope, periodicity and method** are set by the Audit Committee or Board in consultation with him. Existing companies complied within **6 months**. [SM 63–64]

## 6 Appointing the statutory auditor (s.139) · Jun'26 Q3(b)

**FIRST AUDITOR (non-Govt)** the **Board** appoints within **30 days** of registration; till the first AGM [SM 67] → **BOARD FAILS** it tells the members; they appoint at an **EGM within 90 days**; till the first AGM [SM 67] → **AT THE FIRST AGM** members appoint an individual or firm from the end of the 1st AGM **till the end of the 6th AGM**, and so on [SM 64] → **CONSENT + CERTIFICATE** written consent, and a certificate that he is eligible, within limits, and with pending proceedings listed (s.141) [SM 65] → **ADT-1** the company tells the auditor and files ADT-1 with the ROC within **15 days** of the meeting [SM 65]

**Selection (Rule 3):** the **Audit Committee** (or the Board if there is none) weighs qualifications, experience and pending proceedings, and recommends. If the Board agrees, it recommends to members. If not, it refers back with reasons; if the AC holds firm, the Board records its reasons and sends **its own recommendation** to the AGM. Appointment includes re-appointment. [SM 64–65]

### TERM LIMITS + ROTATION s.139(2)–(4)

- **Who is covered:** listed companies; unlisted public companies with paid-up capital ≥ **₹10 crore**; private companies ≥ **₹20 crore**; any company with borrowings or public deposits ≥ **₹50 crore**. **Not** OPCs or small companies. [SM 65–66]
- An **individual**: at most **one term of 5 consecutive years**. An **audit firm**: at most **two terms of 5 consecutive years**. [SM 65]
- **Cooling-off: 5 years** before re-appointment in the same company. A firm with a **common partner** with the outgoing firm is barred for 5 years. A firm in the **same network** (brand, trade name, common control) is not eligible. If the signing partner retires and joins another firm, that firm is barred for **5 years**. A **break of 5 years** counts as rotation. [SM 66]
- Members may resolve to rotate the **audit partner and team**, or to have **joint auditors**. Removal and resignation rights are not affected. [SM 66]

### CASUAL VACANCY · RE-APPOINTMENT

- **Casual vacancy:** the Board fills it within **30 days**. If it arose from **resignation**, a **general meeting** within **3 months** of the Board's recommendation must approve. He holds office **till the next AGM** (MCQ bank 263). [SM 67]
- **A retiring auditor is re-appointed** unless he is disqualified, has refused in writing, or a **special resolution** appoints someone else or says he shall not be re-appointed. If no auditor is appointed, the existing one continues. [SM 68]
- Where an Audit Committee is required, all appointments, including casual vacancies, take its **recommendation** into account. [SM 68]

### GOVERNMENT COMPANIES: THE CAG APPOINTS (s.139(5), (7), (8)) · MQP MCQ

- For a Government company, or any company owned or controlled by the CG or State Government(s), the **CAG** appoints the auditor within **180 days** of the start of the financial year, till the AGM. [SM 67]
- **First auditor:** the CAG within **60 days** of registration → else the Board within the next **30 days** → else members at an EGM within **60 days**. [SM 67]
- **Casual vacancy:** the CAG within **30 days** (MCQ bank 264) → else the Board within the next **30 days**. [SM 67]
- **Deemed Government company:** at least **51%** of paid-up capital held by Governments, Government companies or Government corporations, in any combination. [SM 68]

## 7 Removal and resignation of the auditor (s.140) · Jun'23 Q8(a), Dec'25 and MQP MCQ cases

**1 · BOARD RESOLUTION** to remove him before his term ends → **2 · CG APPROVAL** application in **ADT-2** within **30 days** of the Board resolution [SM 68] → **3 · HEARING** the auditor gets a **reasonable opportunity of being heard** [SM 68] → **4 · SPECIAL RESOLUTION** at a general meeting within **60 days** of the CG's approval; filed in MGT-14 [SM 68]

**RESIGNATION s.140(2), (3)**

- He files **ADT-3** with the **company and the ROC** within **30 days** of resigning, with the facts and reasons. For Government companies, also with the **CAG**. [SM 68–69]
- **Penalty for not filing: ₹50,000** or his remuneration, **whichever is lower**, plus **₹500 a day**, up to **₹2 lakh**. [SM 69]
- The resulting casual vacancy: the Board fills it in 30 days, approved by a general meeting within 3 months (part 6). [SM 67]

**NOT RE-APPOINTING A RETIRING AUDITOR: SPECIAL NOTICE s.140(4)**

- If he has not completed **5 years** (or **10**), a resolution to appoint someone else or not to re-appoint him needs **special notice**; a copy is sent to him. [SM 69]
- His **written representation** is mentioned in the notice and sent to members. If it arrived too late, it is **read out at the meeting**, and he may also be heard. If not circulated, it is **filed with the ROC**. [SM 69]

## 8 Who can be an auditor (s.141) and his fees (s.142)

**Qualified:** only a **chartered accountant** (*SM MCQ 30 = Jun'26 MCQ: a practising CA*), or a **firm (or LLP)** whose **majority of partners practising in India** are CAs. Only the CA partners act and sign for the firm. [SM 69]

| # | Disqualified, s.141(3) |
|---|---|
| a | a **body corporate**, except an LLP [SM 69] |
| b–c | an **officer or employee** of the company, or a **partner or employee** of one [SM 69–70] |
| d | he, his partner or a relative: **holds securities** of the company or its group (a **relative may hold up to ₹1 lakh** face value; any excess is corrected within **60 days**) · is **indebted above ₹5 lakh** to it · has given a **guarantee above ₹1 lakh** for a third party's debt to it [SM 70] |
| e | has a **business relationship** with the company or its group. Allowed: professional services the law permits, and arm's-length ordinary-course dealings such as **telecom, airlines, hospitals, hotels** [SM 70] |
| f | a **relative is a director or KMP** of the company [SM 70] |
| g | is in **full-time employment elsewhere**, or already holds **more than 20 company audits** (not counting OPCs, dormant companies, and private companies with paid-up capital below **₹100 crore**) [SM 70] |
| h | was **convicted of fraud** and **10 years** have not passed [SM 70] |
| i | renders any **s.144 prohibited service** to the company, its holding or its subsidiary [SM 70] |

**Vacation:** an auditor who becomes disqualified is deemed to have **vacated**, which creates a casual vacancy. [SM 71] · **Fees (s.142):** fixed in general meeting or as it decides; the **Board** fixes the first auditor's. They include expenses and facilities, **not** fees for other services. [SM 71]

## 9 Powers and duties of the auditor; fraud reporting (s.143)

**POWERS s.143(1)**

- **Access at all times** to the books and vouchers, wherever kept. [SM 71]
- Right to **information and explanations** from officers. [SM 71]
- **Must inquire:** (1) are loans on security properly secured and on fair terms? (2) do mere book entries harm the company? (3) were shares and securities sold below cost (non-investment, non-banking companies)? (4) are loans shown as deposits? (5) are personal expenses charged to revenue? (6) was cash really received for shares "allotted for cash"? [SM 71]
- The holding company's auditor may **access the subsidiaries' records** for consolidation. [SM 71]

**DUTIES s.143(2)–(4), (9)**

- Reports **to the members** (*SM MCQ 35: shareholders*) whether the FS give a **true and fair view**. [SM 72]
- The report also states: whether all information was obtained; whether **proper books** were kept and branch returns received; whether the FS **agree with the books**; whether they comply with AS; adverse observations; any director **disqualified under s.164(2)**; qualifications; **internal financial controls**. Rule 11 adds: **pending litigation**, foreseeable losses on long-term contracts and derivatives, and delays in transfers to the **IEPF**. [SM 72–73]
- Any "no" or qualified answer must **give the reason**. He follows the **auditing standards** (CG on ICAI's recommendation, after NFRA). [SM 73]

### Fraud reporting by the auditor, s.143(12) + Rule 13 · Dec'25 Q5(a) [SM 73–74]

**1 · REASON TO BELIEVE**
a fraud by officers or employees, of the prescribed amount, in the course of his duties [SM 73]

→

**2 · TO BOARD / AC**
report **immediately**, asking for their reply within **45 days** [SM 73]

→

**3 · TO THE CENTRAL GOVT**
his report + their reply + his comments within **15 days** of the reply (if no reply: his report + a note). Overall **within 60 days** of knowing [SM 73]

→

**4 · FORM**
a statement in **ADT-4**, now filed **electronically only** (Jun'26 supplementary) [SM 73] [Supp Jun'26 p.3]

- **Good faith:** reporting does not breach any duty (s.143(13)). [SM 73]
- It applies equally to the **cost accountant** (cost audit) and the **CS in practice** (secretarial audit) (s.143(14)), and to **branch auditors** for their branch. [SM 74–75]
- **Not reporting:** fine **₹1 lakh** (unlisted company) or **₹5 lakh** (listed). [SM 74]
- Frauds **not reportable** to the CG are disclosed in the **Board's report** (part 3, item d). [SM 57]

**⚠ OLD SM TEXT, AND A THRESHOLD THE SM LEAVES OUT**

The SM still describes a **sealed cover by registered post / speed post on the auditor's letterhead**. The **Jun'26 supplementary** removed that: ADT-4 is now filed electronically and postal submission is discontinued. Write the e-form version. [Supp Jun'26 p.3]

The SM says only "amount as may be prescribed". Rule 13 sets it: a fraud of **₹1 crore or more** is reported to the CG; a smaller one goes to the Audit Committee or Board and is disclosed in the Board's report.

**GOVERNMENT COMPANIES s.143(5)–(7)**

The CAG appoints the auditor and **directs how** to audit. The report covers the CAG's directions, action taken and the impact. Within **60 days** of the report the CAG may conduct a **supplementary audit** and comment; the comments go to members and the AGM. The CAG may also order a **test audit**. [SM 74]

**BRANCH AUDIT s.143(8)**

**Indian branch:** the company's auditor or another qualified person. **Foreign branch:** the company's auditor, an accountant, or a person qualified under that country's law. The branch auditor reports to the company's auditor, who deals with it in his report. [SM 74–75]

## 10 Prohibited services, signing, attending, penalties, cost audit (s.144–148)

**s.144: THE AUDITOR SHALL NOT RENDER (directly or indirectly, to the company, its holding or subsidiary)**

1. **accounting and book-keeping**
2. **internal audit**
3. design and implementation of a **financial information system**
4. **actuarial** services
5. **investment advisory**
6. **investment banking**
7. **outsourced financial services**
8. **management services**
9. any other prescribed service

Other services need **Board or Audit Committee approval**. "Indirectly" covers services through a relative, connected person, partner, or a parent, subsidiary or associate entity, or any entity using his name, brand or trade mark. *SM MCQ 38: none of internal audit, book-keeping or investment advice. SM MCQ 79: he may be the tax auditor.* [SM 75]

**s.145–147**

- **s.145:** he **signs** the report (only CA partners sign for a firm). Qualifications or adverse comments are **read at the general meeting** and are **open to inspection** by members. [SM 76]
- **s.146:** he receives all **notices of general meetings**; he **attends** (or a qualified representative does) unless exempted, and has the **right to be heard**. [SM 76]
- **s.147 company: ₹25,000 to ₹5 lakh**; **officers** ₹10,000 to ₹1 lakh. [SM 76]
- **Auditor** (breach of s.139, 144, 145): **₹25,000 to ₹5 lakh** or **4×** his fee, whichever is lower. **Wilfully, to deceive:** up to **1 year** in jail and a fine of **₹50,000 to ₹25 lakh** or **8×** his fee, whichever is lower. If convicted, he **refunds his fee** and pays damages. [SM 76]
- **Audit firm:** if a partner acted fraudulently, the partner and the firm are **jointly and severally liable**. Non-monetary criminal punishment falls only on the guilty partners. [SM 77]

**s.148 Cost audit:** the CG may order specified companies (by product or service, net worth or turnover) to keep **cost records** (Form **CRA-1**) and to have them audited. The audit is by a **practising cost accountant**, appointed by the **Board** on the Audit Committee's recommendation, with the fee **ratified by shareholders**. It is in addition to the s.143 audit. [SM 77]

## 11 CARO 2020 (never asked yet) · and a CSR pointer

### WHAT IT IS · WHO IS OUT

- The Companies (Auditor's Report) Order, 2020: **extra matters the statutory auditor reports**. Issued on 25 Feb 2020 with NFRA, replacing CARO 2016, and deferred by a year, so it applies from **FY 2020-21**. It covers foreign companies too. [SM 77]
- **Outside CARO:** banking, insurance and **section 8** companies, **OPCs**, **small companies**, and private companies (not holding or subsidiary of a public company) with capital + reserves ≤ **₹1 crore**, bank borrowings ≤ **₹1 crore** and revenue ≤ **₹10 crore**. [SM 78]

**⚠ TWO UPDATES**

**Small company**: the SM gives ₹4 cr capital / ₹40 cr turnover (up to a ceiling of ₹10 cr / ₹100 cr). The **Dec'26 supplementary** sets it at capital ≤ **₹10 crore** and turnover ≤ **₹100 crore** from 1 Dec 2025. [Supp Dec'26 p.2]
**SM MCQ 36** "CARO 2020 is effective from": the MCQ bank key says 1.4.2021, but the SM text says it applies to **FY 2020-21**, which starts **1.4.2020**. Trust the SM text. [SM 77–78]

### CLAUSE 3: WHAT THE AUDITOR REPORTS ON

i. **PPE**: records, physical verification, title deeds, revaluation (10%+ change), **benami** proceedings
ii. **Inventory**: verification (10%+ discrepancy); working capital limits above **₹5 crore**
iii. **loans and guarantees given**: terms, repayment, overdue above **90 days**
iv. compliance with **s.185 and s.186**
v. **deposits**: s.73–76 and RBI directions
vi. **cost records** maintained
vii. **statutory dues**: arrears above **6 months**; disputed dues and forum
viii. income **surrendered in tax assessments** but not in the books
ix. **defaults** on loans
x. use of **IPO/FPO money and term loans**
xi. **fraud** noticed or reported under s.143(12)
xii. **Nidhi** company: NOF to deposits **1:20**, **10%** unencumbered deposits
xiii. **RPTs** under s.188
xiv. **internal audit** system
xv. **non-cash transactions** with directors (s.192)
xvi. **RBI registration** (s.45-IA)
xvii. **cash losses** this year and last
xviii. **auditor's resignation**: were the outgoing auditor's concerns considered?
xix. **material uncertainty**: can it meet liabilities due within **1 year**?
xx. **unspent CSR** transferred (fund / special account)
xxi. CARO **qualifications in group companies** (consolidated FS)

[SM 78–81]

### CSR (s.135) ALSO SITS ON SM 60: FULL NOTES WITH TOPIC 3.4

Applies with net worth ≥ **₹500 crore**, turnover ≥ **₹1,000 crore**, or net profit ≥ **₹5 crore** in the preceding year. A CSR committee of **3** or more directors, at least one an ID. Spend at least **2%** of the average net profit of the last **3 years** (s.198), preferring local areas. Unspent, not ongoing: transfer to a Schedule VII fund within **6 months**. Ongoing project: transfer to a special account within **30 days**, to use within **3 years**. [SM 60]

## 12 Model answers and the auditor MCQ case set

**MODEL ANSWER 1 · REMOVAL / RESIGNATION / QUALIFIED REPORT (JUN'23 Q8(a), 10 MARKS · OUR TOP 1.4 PREDICTION)**

**Facts:** the MD of ABC Ltd wants to remove the auditor, who is unhappy with management's explanations and threatens to resign. Advise on (i) removal, (ii) resignation, (iii) a qualified report.

**(i) Removal (s.140(1)).** The auditor can be removed before his term ends only by a **special resolution** after the **prior approval of the Central Government**. **Procedure:** (1) Board resolution; (2) application to the CG in **ADT-2** with fees within **30 days** of the Board resolution; (3) the auditor is given a **reasonable opportunity of being heard**; (4) general meeting within **60 days** of the CG's approval to pass the special resolution, filed in MGT-14. Note: disagreement over explanations is no ground in itself; the CG must be satisfied. [SM 68]

**(ii) If he resigns (s.140(2), (3)).** He files **ADT-3** with the company and the ROC within **30 days**, stating the facts and reasons (with the CAG too for a Government company). Default: ₹50,000 or his fee, whichever is lower, + ₹500 a day up to ₹2 lakh. The Board fills the casual vacancy within **30 days**, and a general meeting must approve within **3 months**. His reasons become public, so resignation does not make the issues disappear. [SM 67–69]

**(iii) Qualified report.** He states the **reasons** for every qualification (s.143(4)). The Board must give its **explanations or comments on every qualification** in the Board's report (s.134(3)). The qualifications are **read at the general meeting** and are **open to inspection** by members (s.145). [SM 57–76]

**Advice to the MD:** removal is slow and needs Government approval and a hearing. The proper course is to answer the auditor's points. If the qualifications stand, the Board must explain them to the members.

**MODEL ANSWER 2 · FRAUD REPORTING BY AUDITORS (DEC'25 Q5(a), 7 MARKS · NOW WITH THE JUN'26 AMENDMENT)**

1. **Provision:** under s.143(12), if the auditor, in the course of his duties, has **reason to believe** that a fraud of the prescribed amount is being or has been committed in the company **by its officers or employees**, he reports it to the **Central Government** within **60 days** of knowing. [SM 73]
2. **Step 1:** he sends his report to the **Board or Audit Committee immediately**, seeking their reply or observations within **45 days**. [SM 73]
3. **Step 2:** within **15 days** of their reply, he forwards his report, their reply and his comments to the CG. If no reply comes in 45 days, he sends his report with a note saying so. [SM 73]
4. **Form:** a statement in **ADT-4**, filed **electronically** on the MCA portal (the postal mode was discontinued by the 2025 amendment, Jun'26 supplementary). [Supp Jun'26 p.3]
5. **Protection and extension:** a report made in **good faith** breaches no duty. The same applies to **cost auditors, secretarial auditors and branch auditors**. [SM 73–75]
6. **Penalty for not reporting:** ₹1 lakh (unlisted) or ₹5 lakh (listed). Frauds below the CG threshold are disclosed in the **Board's report**. [SM 57–74]

**THE AUDITOR MCQ CASE SET (DEC'25 Q1 (i)–(iv); ICMAI MQP REPEATED IT): HIGHWAY LTD**

**Facts:** three State Governments hold **15% each (45%)**. Mr Parimal, CA, was appointed auditor by ordinary resolution; members objected that the CAG's approval and a special resolution were needed. He resigned mid-term; the Board appointed another auditor 10 days later.

| Question | Answer and reason |
|---|---|
| Is it a Government company, so that the CAG appoints? | **No**: Governments hold 45%, below the **51%** needed. Members appoint at the AGM by ordinary resolution; the objection fails. [SM 68] |
| He resigned without ADT-3: penalty? | ₹50,000 or his fee (₹2 lakh), **whichever is lower = ₹50,000**, + ₹500 a day up to ₹2 lakh. [SM 69] |
| The new auditor owes the company ₹2 lakh (MQP: ₹1.5 lakh): eligible? | **Yes**: the debt limit is **₹5 lakh** (Dec'25 option A). [SM 70] |
| Charged with a ₹1.5 crore fraud, not convicted: can he continue? | **Yes, unless convicted**: the bar is a conviction for fraud within **10 years** (option B). [SM 70] |
| Board appointed the new auditor after a resignation | valid if done within **30 days**, but a **general meeting must approve within 3 months**. [SM 67] |

⚠ Q(iv) on fees for incomplete work turns on the terms of appointment; the SM has no rule. Our reading: option D, reasonable fees for work done, subject to the terms. Check against ICMAI's suggested answer.

## SM exercise and MCQ-bank questions on 1.4, with answers (SM 162–172)

| | | | |
|---|---|---|---|
| 27 practising CA as auditor: term | **5 years** | 34 private co internal auditor if turnover | **₹200 cr or more** |
| 28 Directors' Responsibility Statement is part of | **Board's report** | 35 auditor's report is addressed to | **shareholders** |
| 29 NFRA | **National Financial Reporting Authority** | 36 CARO 2020 effective from | **FY 2020-21 (1.4.2020)** ⚠ |
| 30 statutory auditor shall be ★ | **practising CA** | 37 first auditor appointed by | **Board of Directors** |
| 31 Board's report signed by ★ | **chairman with Board's authority** | 38 extra service the auditor may render | **none of internal audit, book-keeping, investment advice** |
| 32 CAG | **Comptroller and Auditor General** | 79 statutory auditor can also be | **tax auditor** |
| 33 FS filed with ROC within | **30 days of AGM** | 89 books inspected by ★ | **any director** |
| 90 accounting standards prescribed by | **Central Government** | bank 231: OPC files FS within | **180 days (6 months)** |
| bank 259: notice of auditor's appointment | **ADT-1** | bank 263: casual-vacancy auditor holds till | **next AGM** |
| bank 264: CAG fills casual vacancy within | **30 days** | bank 265: resigning auditor files | **ADT-3 in 30 days** |
| bank 304: DRS is in section | **134(3)(c)** | bank 303: non-compliance with AS: disclose | **deviation, reasons, effect** |

## R Revision: every number in 1.4

| Rule | Number |
|---|---|
| books elsewhere in India: notice to ROC | 7 days |
| foreign records: returns to RO / director's request | quarterly / 15 days |
| preserve books for | 8 FYs |
| s.128 fine | ₹50,000–₹5 lakh |
| first FY if incorporated on/after | 1 January |
| s.129 contravention: jail / fine | 1 yr / ₹50,000–₹5 lakh |
| s.129A results filed within | 30 days |
| Board evaluation statement: public paid-up | ₹25 crore |
| s.134 penalty: company / officer | ₹3 lakh / ₹50,000 |
| POSH complaints pending more than | 90 days |
| FS copies before meeting / s.8 company | 21 / 14 days |
| shorter notice consent | 95% |
| e-mode: net worth / turnover above | ₹1 cr / ₹10 cr |
| s.136 penalty: company / officer | ₹25,000 / ₹5,000 |
| s.137 filing after AGM / OPC | 30 days / 180 days |
| late filing with fees up to | 270 days |
| s.137 penalty company: base / day / max | ₹10,000 / ₹100 / ₹2 lakh |
| s.137 officers: maximum | ₹50,000 |
| internal audit (unlisted public): capital / turnover | ₹50 cr / ₹200 cr |
| internal audit: bank loans / deposits | > ₹100 cr / ₹25 cr |
| internal audit (private): turnover / loans | ₹200 cr / > ₹100 cr |
| CSR: net worth / turnover / profit | ₹500 / ₹1,000 / ₹5 cr |
| CSR spend / unspent fund / special a/c | 2% / 6 months / 30 days |

| Rule | Number |
|---|---|
| first auditor: Board / EGM | 30 / 90 days |
| auditor term: 1st AGM till | 6th AGM |
| ADT-1 filed within | 15 days |
| rotation: individual / firm | 1 × 5 yrs / 2 × 5 yrs |
| rotation covers: unlisted public / private / borrowings | ₹10 cr / ₹20 cr / ₹50 cr |
| cooling-off / break counts as rotation | 5 yrs / 5 yrs |
| casual vacancy: Board / GM if resignation | 30 days / 3 months |
| CAG: appoint / first auditor / casual | 180 / 60 / 30 days |
| deemed Government company | 51% |
| removal: ADT-2 within / GM within | 30 / 60 days |
| resignation ADT-3 within | 30 days |
| no ADT-3: penalty / day / max | ₹50,000 or fee / ₹500 / ₹2 lakh |
| special notice if term not completed | 5 or 10 yrs |
| relative's holding / correct within | ₹1 lakh / 60 days |
| auditor's debt / guarantee limit | ₹5 lakh / ₹1 lakh |
| audit ceiling / private-co exclusion | 20 / < ₹100 cr |
| fraud conviction bar | 10 years |
| fraud: Board reply / to CG / overall | 45 / 15 / 60 days |
| fraud non-reporting: unlisted / listed | ₹1 lakh / ₹5 lakh |
| CAG supplementary audit within | 60 days |
| s.147 company / officers | ₹25,000–₹5 lakh / ₹10,000–₹1 lakh |
| auditor: fine or × fee / wilful | ₹5 lakh or 4× / ₹25 lakh or 8× |
| CARO private-co exclusion: capital / loans / revenue | ₹1 cr / ₹1 cr / ₹10 cr |
| CARO: discrepancy / WC limit / overdue | 10% / ₹5 cr / 90 days |
| CARO: dues arrears / Nidhi ratio | 6 months / 1:20 |
| small company (Dec'26 supp.) | ₹10 cr / ₹100 cr |

# 1.6 · Board Meetings and Procedures

P13 · Module 1 · Companies Act, 2013 · s.118, 173–177, 182

SM pp. 116–132 (17 pages). 57 marks in 7 papers, with a long question in 5. **Zero in Jun'26**, after three halves in Jun'25 and two in Dec'25: **the strongest "due back" topic in P13.**

| Paper | What was asked | Marks |
|---|---|---|
| Jun'23 | MCQ: Board quorum · Q4(a)(ii) **120-day gap**; approving FS by video meeting; audit committee chairman abroad | 2 + 4 |
| Dec'23 | Q4(a) the Board met **3 times**; the 4th failed for want of quorum: any contravention? | 7 |
| Jun'24 | MCQ: AGM quorum (s.103, not in the SM) · Q3(a) **quorum cases**: 8 of 10, a section 8 company, an interested director with articles fixing 5 | 2 + 7 |
| Jun'25 | Q3(a) **quorum cases again**: 3 of 11; interested directors · Q5(a) **audit committee** duties; are its recommendations binding? · Q6(a) **registers**: list ten | 7 + 7 + 7 |
| Dec'25 | Q3(a) **shorter notice**, no ID present, venue for a VC meeting · Q4(a) Sunday 8 pm meeting in Mumbai (RO Chennai), notice to a director in London, VC link drops | 7 + 7 |
| Jun'26 | nothing | 0 |

**HOW IT IS EXAMINED**

- **Calculation cases on quorum** (asked twice; in both ICMAI's MQP and PTP). Learn the **quorum calculator** on page 3 and the model answer.
- **Notice, shorter notice and video conferencing** cases: 4 times. Answer each sub-question as provision → facts → conclusion.
- Theory 7-markers: **audit committee**, **registers**. Not yet asked: circular resolutions, minutes, directors' duties, and **political contributions** (ICMAI PTP).

**DEC'26: OUR PREDICTION (A PREDICTION, NOT A PROMISE)**

Tier **A**. Expected **7–14 marks**. Our model gives it the **highest chance (100%) of being the 4-MCQ case set** in Q1, plus a 7-mark case. Likely questions:

1. Quorum with interested directors: 3 present of 11 (MQP + PTP)
2. Notice, shorter notice, ID's role, video conferencing (s.173(3)) (MQP)
3. Political contributions: conditions, limits, disclosure (s.182) (PTP)
4. Circular resolution (s.175) / minutes (s.118) / duties (s.166): never asked yet

**MAP OF THIS PACK**

1. How often the Board meets (s.173(1)) ★★
2. Video conferencing and notice (s.173(2)–(4)) ★★★
3. Quorum (s.174) + calculator ★★★
4. Resolution by circulation (s.175) ★
5. Minutes (s.118, 119) ★
6. Registers (s.94) ★★
7. Board composition and committees; audit committee and vigil mechanism (s.177) ★★
8. Duties (s.166) and liabilities of directors ★
9. Political contributions (s.182) ★★
10. Model answers · numbers · SM MCQs

## 1 How often the Board must meet (s.173(1))

**FIRST MEETING**
within **30 days** of incorporation [SM 116]

→

**EVERY YEAR**
at least **4 meetings** [SM 116]

→

**GAP**
no more than **120 days** between two consecutive meetings [SM 116]

→

**OPC / SMALL / DORMANT**
at least **one meeting in each half** of the calendar year, at least **90 days** apart (not for an OPC with one director) [SM 116]

Under the Secretarial Standards, committees meet as often as needed, and **independent directors meet separately at least once a calendar year** (SM MCQ 56). A company may convene a meeting at **any time and place, on any day except a national holiday** (26 January, 15 August, 2 October, and days the CG declares). [SM 116–118]

**⚠ NOT IN THE SM: A MEETING WITHOUT QUORUM (needed for Dec'23 Q4(a))**

Under **s.174(4)**, if a Board meeting cannot be held for want of quorum, then unless the articles say otherwise it **stands adjourned to the same day next week**, at the same time and place (or the next day if that is a national holiday). **Dec'23 answer:** the 4th meeting could have been held on the adjourned date. With only 3 meetings in the year, **s.173(1) (at least 4 meetings) is contravened**, and the 120-day gap may also have been crossed.

## 2 Video conferencing and notice of the meeting (s.173(2)–(4))

**ATTENDING BY VIDEO (s.173(2), RULE 3)**

- Directors may attend **in person, by video conferencing, or by other audio-visual means** that can record and recognise participation and record and store the proceedings with date and time. [SM 116–117]
- The company arranges against connection failure. The **chairperson and CS** ensure security and identification, proper equipment, recording and minutes, storage of recordings (at least until that year's audit is complete), that only the director concerned attends, and that everyone can see and hear clearly. [SM 117]
- A differently-abled director may ask to bring a person along. [SM 117]
- Directors on video **count for quorum**. [SM 118]

**VENUE AND INTIMATION (RULE 3)**

- The notice states the **video option** and how to use it. A director who wants it tells the chairperson or CS in advance; a declaration at the start of the calendar year is valid for **one calendar year**. If he says nothing, he is **assumed to attend in person**. [SM 117–118]
- **Venue (Dec'25 Q3(a)(iii)):** a notice offering video participation must name a **venue**, and that is the place where **all recordings of the proceedings are made**. [SM 118]

**⚠ "MATTERS THAT CANNOT BE DONE BY VIDEO" (Jun'23 Q4(a)(ii); one of our Dec'26 picks)**

The SM says only that the CG "may restrict" matters for video meetings. That list (Rule 4: approving annual FS and the Board's report, prospectus, mergers, etc.) was **omitted in 2021**, so today **any matter, including approving the annual FS, may be taken up by video**. In an answer, state the s.173(2) power, then that the restricted list no longer applies. [SM 117]

### Notice of a Board meeting, s.173(3) + SS-1 [SM 117–118]

**THE RULE**

- At least **7 days' notice in writing** to **every director** at his registered address, **in India or abroad**, by **hand, post or electronic means**. A director abroad (Dec'25 Q4(a)(ii)) gets it the same way, usually by e-mail. [SM 117]
- **Shorter notice** for **urgent business** only: at least **one independent director** (if the company has one) must be present. If none is present, decisions are **circulated to all directors** and become **final only when at least one ID ratifies**. The notice must say it is at shorter notice. [SM 117]
- **Penalty** for failing to give notice: **₹25,000** on every officer whose duty it was. [SM 118]

**SS-1 DETAILS**

- sent by the **means the director specified**; issued by the **CS** (or a director or authorised person) [SM 118]
- states the **serial number, day, date, time and full address of the venue**, plus the video option and a contact [SM 118]
- **agenda and notes on agenda** go with the notice; meetings and items are **serially numbered**; **proof of sending** is kept [SM 118]
- any time, any place, any day except a **national holiday** [SM 118]

## 3 Quorum (s.174) and the quorum calculator

**WHAT IT IS** The **quorum** is the minimum number of directors who must be present for business to be validly done. Without it, the meeting is not properly held. [SM 118]

- **One-third of total strength, or 2, whichever is higher** (SM MCQ 57 = Jun'23 MCQ). [SM 118]
- A **fraction counts as one** (3.33 → 4). [SM 119]
- **Total strength excludes vacant places.** [SM 119]
- Directors on **video count**. [SM 118]
- An **interested director** (s.184) does not count for that item. If interested directors are **two-thirds or more of total strength**, the quorum is the **non-interested directors present, at least 2**. [SM 119]
- If directors fall below the quorum, the **continuing directors** may act **only to bring the number up to the quorum or to call a general meeting**. [SM 119]
- **Section 8 company: 8** members or **25%** of total strength, **whichever is less**, but not less than **2**. [SM 119]
- Not for an OPC with one director. The quorum must be present **throughout** the meeting (SS-1). A committee needs **all** its members unless provided otherwise. [SM 119]

**1 · TOTAL STRENGTH** sanctioned directors minus vacancies → **2 · ⅓, ROUND UP** compare with 2; take the higher. Section 8: lower of 8 and 25% (minimum 2) → **3 · ARTICLES** if the articles fix a higher number, use it → **4 · PER ITEM** leave out interested directors present. If interested ≥ ⅔ of strength: quorum = disinterested present (≥ 2) → **5 · VERDICT** meeting valid? each item valid? if not, adjourn or defer the item

| Exam case (Jun'24 Q3(a), Jun'25 Q3(a), MQP, PTP) | Working | Verdict |
|---|---|---|
| public company, 10 directors, 8 present | 10/3 = 3.33 → **4** (higher than 2); 8 ≥ 4 | **valid** |
| section 8 company, 8 directors, 3 present | lower of 8 and 25% × 8 = 2 → **2**; 3 ≥ 2 | **valid** |
| 12 directors, 9 present, articles fix 5, one present director interested in an item | Act: 12/3 = **4**; articles raise it to **5**. For that item: 9 − 1 = 8 disinterested ≥ 5 | **valid** |
| 11 directors, 3 present, none interested | 11/3 = 3.67 → **4**; 3 < 4 | **no quorum**: adjourned |
| 11 directors, 5 present; only 2 present are not interested in one item | quorum **4** (interested are fewer than ⅔ of 11 = 7.33, so the normal rule applies). For that item only **2** count: below 4 | meeting valid; **that item deferred** |

If the facts said 8 or more of the 11 directors were interested (two-thirds or more), the special rule applies and the 2 disinterested present would be enough.

## 4 Resolution by circulation (s.175): never asked yet

**HOW IT IS PASSED**

1. The **draft resolution with papers** is circulated to **all directors** (or committee members) at their registered addresses, by hand, post, courier or electronic means. [SM 119]
2. It is **approved by a majority** of directors entitled to vote. [SM 119]
3. If **one-third** of directors want it decided at a meeting, the chairperson must put it to a meeting (SM MCQ 58). [SM 119]
4. It is **noted at the next Board meeting** and made part of its minutes. [SM 120]
5. SS-1: directors get **at most 7 days** from circulation to respond. [SM 120]

**NOT BY CIRCULATION (SS-1 Annexure A, selected)**

**General:** noting committee minutes · approving **FS and the Board's report** · compliance certificate · list of applicable laws · appointing secretarial and internal auditors. **Specific:** borrowing (other than debentures), investing, loans and guarantees, **political contributions**, calls, MD/WTD pay, KMP appointment, MD of two companies, casual vacancies, non-arm's-length RPTs, selling subsidiaries, material assets, payment for loss of office. **Corporate actions: buy-back** (SM MCQ 63), issue of securities, mergers, diversification, takeovers. [SM 120–121]

## 5 Minutes (s.118, s.119)

- Minutes of every **general meeting**, **postal ballot** resolution, **Board meeting** and **committee meeting** are prepared, signed and kept within **30 days** of the meeting, in books with **consecutively numbered pages**. [SM 121]
- They contain a **fair and correct summary** and all **appointments**. Board minutes also record the **directors present** and the **dissenting directors**. [SM 121–122]
- The **chairman** may leave out matter he considers **defamatory, irrelevant or immaterial, or detrimental** to the company; his discretion is absolute. [SM 121–122]
- Signed by the chairman of **that meeting or the next** (SM MCQ 59). Draft minutes are circulated to directors within **15 days**. Board minutes are kept **permanently** at the **registered office** (SM MCQs 60, 61). [SM 121–122]
- Minutes are **evidence**: the meeting is deemed duly held and appointments valid, until the contrary is proved. Reports of general meetings may not be circulated at the company's expense. [SM 122]
- **Secretarial Standards** (SS-1 Board, SS-2 general meetings) must be observed (s.118(10)). [SM 122]
- **s.119:** general meeting minutes are kept at the RO and open to **members free of charge**, at least **2 hours** each business day. A copy is given within **7 days** of a request, on payment of fees. [SM 122]
- **Default:** company **₹25,000**, each officer **₹5,000**. [SM 122]

## 6 Registers to be maintained (Jun'25 Q6(a): "enumerate any ten")

| Register | Section · form | Register | Section · form |
|---|---|---|---|
| investments not held in the company's name | 187(3) · MBP-3 | members (+ index) | 88(1)(a) · MGT-1 |
| deposits | 73 · Rule 14 | debenture holders (+ index) | 88(1)(b) · MGT-2 |
| securities bought back | 68(9) · SH-10 | beneficial owners | 88 |
| charges | 85(1) · CHG-7 | foreign register of members | 88 · MGT-3 |
| contracts in which directors are interested | 189(1) · MBP-4 | copies of annual returns | 94(1) |
| directors and KMP | 170(1) | minute books | 118 |
| loans, investments, guarantees | 186(9) · MBP-2 | postal ballot | 110 |
| renewed and duplicate share certificates | Rule 6 · SH-2 | books of account; cost records | 128 |
| sweat equity shares | 54 · SH-3 | [SM 123] | |

**Where:** at the **registered office**. They may be kept elsewhere in India where **more than 10%** of members live, by **special resolution**, with an advance copy to the ROC. **Inspection:** members, debenture holders and beneficial owners **free**; others for a fee; extracts free, copies for a fee. Electronic maintenance is allowed; **SS-4** on registers is recommendatory. [SM 123–124]

**Powers and restrictions (s.179, s.180)** repeat on SM 124–126: see **1.5 part 7**. One extra point here: a **borrowing beyond the s.180 limit** is not valid **unless the lender proves** he lent in **good faith** without knowing the limit was exceeded. [SM 126]

## 7 Board composition, committees, audit committee and vigil mechanism (s.177) · Jun'25 Q5(a)

**LISTED COMPANY BOARD (LODR Reg 17)**

- A mix of executive and non-executive directors, with at least **one woman** and at least **50% non-executive**. [SM 126]
- **Non-executive chairman:** at least **one-third** IDs. **Executive chairman:** at least **half** IDs (SM MCQ 64). [SM 126]
- At least **4 Board meetings** a year, gap at most **120 days**. A director may sit on at most **10 committees** and chair at most **5**. Disclosures: an MD&A report, a corporate governance report, and the **auditor's certificate** on governance compliance. [SM 128]

**COMMITTEES (SM table)**

| Committee | Composition | Chair |
|---|---|---|
| Audit | at least **3**, majority IDs | ID |
| Nomination & Remuneration | at least **3**, all non-executive, at least **50%** IDs | ID |
| Stakeholders Relationship | as the Board decides | non-executive |
| Risk Management | majority Board members | Board member |
| CSR (s.135) | at least **3**, at least one ID (see 3.4) | – |

[SM 127]

### Audit committee, s.177 [SM 128–129]

**WHO MUST HAVE ONE · COMPOSITION**

- Every **listed company**, and every **public company** with paid-up capital ≥ **₹10 crore**, OR turnover ≥ **₹100 crore**, OR loans, debentures and deposits above **₹50 crore** (per the last audited FS). [SM 128]
- At least **3 directors**, **IDs forming a majority** (not needed for section 8 companies). The majority, **including the chairperson**, must be able to **read and understand financial statements**. Its composition is disclosed in the Board's report. [SM 129]

**Are its recommendations binding? No**: they are **recommendatory**. But if the Board **does not accept** one, it must disclose that in the **Board's report with reasons** (MCQ bank 141). [SM 129]

**TERMS OF REFERENCE (the 7-mark list)**

1. recommend the **appointment, remuneration and terms of the auditors** (Government company: remuneration only, as the CAG appoints)
2. review and monitor the auditor's **independence, performance and audit effectiveness**
3. **examine the FS** and the auditor's report
4. **approve RPTs** and later changes (omnibus approval allowed)
5. scrutinise **inter-corporate loans and investments**
6. **valuation** of undertakings or assets where needed
7. evaluate **internal financial controls and risk management**
8. monitor the **end use of funds** raised through public offers

[SM 129]

**Powers:** it may **investigate** these matters, take outside professional advice, and have full access to records. It may call for the **auditors' comments** on internal control, audit scope and the FS, and discuss them with internal and statutory auditors (MCQ bank 140). **Auditors and KMP may be heard** when it considers the audit report, but **cannot vote**. [SM 129]

**VIGIL MECHANISM s.177(9) + RULE 7**

**Who:** listed companies, companies **accepting public deposits**, and companies that borrowed above **₹50 crore** from banks or PFIs. **What:** directors and employees report **genuine concerns**, with safeguards against victimisation and **direct access to the audit committee chairperson** in exceptional cases. It is disclosed on the website and in the Board's report. The audit committee oversees it (conflicted members recuse); where there is no audit committee, the Board **nominates a director** for the role. Repeated frivolous complaints may lead to action, including **reprimand**. [SM 130]

## 8 Duties (s.166) and liabilities of directors: never asked yet

**s.166: A DIRECTOR SHALL …**

a. act according to the **articles**, subject to the Act
b. act in **good faith** to promote the company's objects, in the best interests of the **company, employees, shareholders, community and the environment**
c. use **due and reasonable care, skill and diligence**, and **independent judgment**
d. avoid **conflicts of interest**, direct or indirect
e. not seek **undue gain** for himself, relatives, partners or associates
f. not **assign his office**

Directors are **not agents of the shareholders**; even the group that nominated a director cannot instruct him. *Milan Sen v. Guardian Plasticate*: whether the company needs more capital (a rights issue) is for the directors, and courts do not interfere without mala fides. [SM 130–131]

**LIABLE WHEN …**

- **To outsiders:** contracts **ultra vires** the company or beyond their authority, or made in their own name · a misleading **prospectus** · **fraud** · **irregular allotment** · a court order for **fraudulent trading**. [SM 131–132]
- **To the company: negligence** causing loss · ultra vires acts · illegal acts or **breach of trust**. [SM 132]
- **To shareholders:** as **trustees** of the company's property and powers, they make good losses from breach of trust or negligence. [SM 132]
- **Statutory defaults** under the Act. [SM 132]

## 9 Political contributions (s.182) · ICMAI PTP Q3(a)

**THE RULE AS THE SM GIVES IT**

- A company may contribute, directly or indirectly, to a **political party registered under s.29A** of the Representation of the People Act, 1951. [SM 132]
- **Cannot contribute:** a **Government company**, or a company **less than 3 financial years old**. [SM 132]
- Only by a **resolution at a Board meeting** (not by circulation). [SM 132]
- "Contribution" includes donations or payments likely to affect public support for a party, and spending on **politically connected publications**. [SM 132]
- **Disclose** the amounts contributed in the **profit and loss account**. [SM 132]

**⚠ THE SM SAYS "NO LIMIT": THAT CHANGED IN 2024**

The 2017 amendment removed the old cap. In **February 2024** the Supreme Court (*Association for Democratic Reforms v. Union of India*, the electoral bonds case) **struck down that amendment**. That brings back the limit of **7.5% of the average net profits of the preceding three financial years**, and disclosure of the **party's name**. Write the SM rule, then add this update in one line. [SM 132]

## 10 Model answers: our top two Dec'26 questions on 1.6

**MODEL ANSWER 1 · QUORUM CASE (JUN'25 Q3(a), REPEATED IN ICMAI'S MQP AND PTP) · 7 MARKS**

**Q.** What is the quorum for a Board meeting? (1) Only 3 of 11 directors were present and none was interested. Is the meeting valid? (2) Of 11 directors, 5 were present, but only 2 of them were not interested in one transaction. How should the meeting deal with it?

**Provision (s.174):** the quorum is **one-third of the total strength or two directors, whichever is higher**; a fraction counts as one, and vacant places are excluded. Directors on video count. An **interested director** (s.184) is not counted for the item he is interested in. Where interested directors are **two-thirds or more of total strength**, the quorum is the non-interested directors present, provided they are at least two. The quorum must be present throughout (SS-1). [SM 118–119]

**(1)** Total strength 11 → 11/3 = 3.67 → **quorum 4**. Only 3 are present, so there is **no quorum**. The meeting is **not validly held**; no business can be done, and it stands adjourned (s.174(4)).

**(2)** The quorum is 4, and 5 are present, so the **meeting itself is valid**. For the transaction, only the 2 non-interested directors count. The interested directors present (3) are fewer than two-thirds of 11 (7.33), so the special rule does not apply and the normal quorum of 4 is needed. **2 < 4**, so **that transaction cannot be approved**; it is deferred to a meeting with enough disinterested directors. The interested directors must disclose their interest and stay out of the discussion (s.184).

**Conclusion:** (1) invalid, adjourned; (2) the meeting proceeds with other business; the interested transaction is deferred.

**MODEL ANSWER 2 · NOTICE / SHORTER NOTICE / VIDEO CONFERENCE (DEC'25 Q3(a) + Q4(a)) · 7 MARKS**

1. **Notice (s.173(3)):** at least **7 days' written notice** to every director at his registered address in India or abroad, by hand, post or electronic means. A director in **London** is served at his registered address there, normally **by e-mail**. [SM 117]
2. **Shorter notice:** allowed for **urgent business**, if the notice says so and **at least one independent director is present**. **Without an ID**, decisions may still be taken, but they are circulated to all directors and become **final only on ratification by at least one ID**. [SM 117]
3. **Venue, day, time:** under SS-1 a meeting may be held **at any time and place, on any day except a national holiday**. Sunday 5 January, 8 p.m., at a Mumbai hotel (RO in Chennai) is **valid**: it is not a national holiday, and there is no rule that the meeting must be at the RO. [SM 118]
4. **Video conference venue:** the notice must name a venue, and that is the place where the **recordings of the proceedings are made**. Here, the Mumbai venue. [SM 118]
5. **Quorum:** 14 posts, 2 vacant → strength **12** → quorum **4**. 7 attend (3 in person, 4 by video); video directors count. If the London link drops, **5 remain ≥ 4**, so the meeting continues validly. The quorum must exist **throughout**; the dropped directors are recorded as not present for later items. [SM 118–119]

### SM exercise MCQs on 1.6, with answers (SM 166–171; ★ = asked in an exam)

| | | | |
|---|---|---|---|
| 57 Board quorum ★ | **⅓ or 2, higher** | 61 minutes kept at | **registered office** |
| 58 circular resolution goes to a meeting if asked by | **one-third** of directors | 63 buy-back authorised by Board | **only at a Board meeting** |
| 59 Board minutes signed by | **chairman of that or the next meeting** | 55 / 65 audit committee majority | **independent directors** |
| 60 Board minutes preserved | **permanently** | 56 IDs meet separately, a year | **once** |
| bank 140: audit committee may | **interact with statutory and internal auditors** | bank 141: its recommendation | **if not accepted, Board records reasons** |

## R Revision: every number in 1.6

| Rule | Number |
|---|---|
| first Board meeting within | 30 days |
| meetings a year / maximum gap | 4 / 120 days |
| OPC, small, dormant: per half-year / gap | 1 / ≥ 90 days |
| IDs meet separately | once a calendar year |
| video intimation valid for | 1 calendar year |
| notice of Board meeting | 7 days |
| shorter notice: IDs present | at least 1 |
| penalty for no notice | ₹25,000 per officer |
| quorum | ⅓ or 2, higher |
| interested special rule at | ≥ ⅔ of strength |
| section 8 quorum | 8 or 25%, lower; ≥ 2 |
| circulation: send to meeting if / reply within | ⅓ / 7 days |

| Rule | Number |
|---|---|
| minutes kept within / draft circulated | 30 / 15 days |
| GM minutes: inspection / copy within | 2 hrs a day / 7 days |
| s.118 default: company / officer | ₹25,000 / ₹5,000 |
| registers elsewhere if members there exceed | 10% |
| listed: women / non-executive | 1 / 50% |
| IDs: non-exec / exec chairman | ⅓ / half |
| committees: member / chair, at most | 10 / 5 |
| audit committee: paid-up / turnover / debt | ₹10 cr / ₹100 cr / > ₹50 cr |
| audit / NRC committee size | ≥ 3 / ≥ 3 |
| NRC independent share | ≥ 50% |
| vigil mechanism: bank borrowings above | ₹50 crore |
| political contribution: company age | ≥ 3 FYs |

# 1.1 · Company Formation and Conversion P13 · Module 1 · Companies Act, 2013

SM pp. 3–33 (31 pages). 53 marks in 7 papers, asked in 6 of them, with a long question in 5. The Jun'26 long question was **private → public**, so the reverse, the LLP route or OPC is fresher.

| Paper | What was asked | Marks |
|---|---|---|
| Jun'23 | MCQs: foreign company definition; shifting the RO from one State to another | 4 |
| Dec'23 | MCQ: RO moved to another ROC in the same State → Regional Director · Q4(b) **public → private: counting the 200 members** | 2 + 7 |
| Jun'24 | MCQ: 35% holding but controls the Board → subsidiary · Q5(b) **constructive notice and indoor management, with exceptions** | 2 + 7 |
| Dec'24 | MCQ: RO moved within the city → Board resolution · Q2(a) **OPC: nominee leaves India and withdraws; minor nominee; consequences** | 2 + 7 |
| Dec'25 | MCQ: US company with no business in India · Q4(b) **not-for-profit consulting company: s.8 licence** | 2 + 7 |
| Jun'26 | Q1 (i)–(iii) MCQ case: ultra vires contract, unauthorised borrowing (indoor management), prospectus misstatement · Q4(a) **private → public: procedure** | 6 + 7 |

**HOW IT IS EXAMINED**

- **Conversion cases** (public ↔ private, LLP → company in ICMAI's MQP), **OPC**, **section 8** and the **three doctrines** (ultra vires, constructive notice, indoor management).
- **MCQs come from the SM exercise**: Jun'23 Q1(i) = SM MCQ 5; Jun'24 Q1(i) = SM MCQ 14; Dec'24 Q1(i) = SM MCQ 11; Dec'25 Q1(vi) = SM MCQ 92; Jun'23 Q1(v) = MCQ bank 96.
- **The SM is outdated in places** (OPC, conversion approval, small company): see the ⚠ boxes. The Dec'26 supplementary's **small company** limits are an ICMAI "Examination Point".

**DEC'26: OUR PREDICTION (A PREDICTION, NOT A PROMISE)**

Tier **A**. Expected **7–13 marks**: a 7-mark case plus 1–3 MCQs. Likely questions:

1. LLP converting into a company: procedure and effect (s.366) (MQP)
2. Start-up case: public or private, NRI investor, a section 8 company making profits (PTP)
3. Public → private: the 200-member count and approvals (Dec'23)
4. OPC nominee withdraws / minor nominee (Dec'24)

**MAP OF THIS PACK**

1. What a company is; lifting the veil ★
2. Kinds of companies ★★
3. One Person Company ★★
4. Incorporation, commencement, effect ★
5. Registered office ★★ (MCQs)
6. Memorandum, name, alteration ★
7. Articles; the three doctrines ★★★
8. Conversions: public ↔ private, LLP ★★★
9. Section 8 companies ★★
10. Foreign companies ★
11. Model answers · SM MCQs · numbers

## 1 What a company is, and lifting the corporate veil

**WHAT IT IS** A company is an **artificial, legal, juristic person, separate from its members, with perpetual existence**. Under s.2(20) it is a company incorporated under the Act or a previous company law. The Act has **29 chapters, 470 sections and 7 schedules**, and is administered by the **MCA** through the ROC, NCLT and NCLAT. [SM 3–4]

**FEATURES**

- **Separate legal entity**: *Salomon v. Salomon & Co.* [SM 4]
- **Limited liability**: up to the unpaid nominal value of shares, or the guaranteed amount [SM 4]
- **Perpetual succession**: "members may come and go" (*Gopalpur Tea Co.*) [SM 4]
- **Separate property**: shareholders do not own its assets (*Bacha F. Guzdar v. CIT*) [SM 4]
- **Transferable shares**: movable property, transferable as the articles provide (s.44) [SM 5]
- **Common seal optional** since 2015. Without a seal, documents are authorised by **two directors**, or a director and the CS [SM 5]

**THE VEIL IS LIFTED (courts look at the people behind) ...**

- trading with the **enemy** (test of control) · **taxes**, duties, stamps
- a subsidiary acting as the parent's **agent** (*Smith, Stone & Knight*)
- avoiding **welfare legislation** (*Workmen of Associated Rubber*)
- **fraud** or improper conduct · abuse for an unjust purpose
- **public policy** (*Connors v. Connors*) · **exchange control**, quasi-criminal cases
- using a company to **avoid legal obligations**
- *Estate Officer v. Esys IT* (SC 2016): a share transfer that was really a **prohibited sale of land**

[SM 5–6]

## 2 Kinds of companies

| Basis | Kind and definition |
|---|---|
| Incorporation | **Statutory** (by a special Act, e.g. RBI, SBI, LIC; the Act applies only if that Act says so) · **Registered** (under this Act or earlier ones) [SM 7] |
| Liability | **Limited by shares** s.2(22): liability limited to the **unpaid amount** on shares · **by guarantee** s.2(21): the amount each member undertakes to contribute on winding up (similar to an LLP) · **unlimited** s.2(92): no limit [SM 7–8] |
| Members | **OPC** s.2(62): one member (part 3) · **Private** s.2(68): articles **restrict share transfers**, limit members to **200** (except OPC), and **prohibit public invitation**. Joint holders count as one; **employees and ex-employees who became members while employed are not counted** · **Public** s.2(71): not private; at least **7** members. A **subsidiary of a public company** is deemed public [SM 8–9] |
| Size | **Small company** s.2(85): a non-public company within the capital and turnover limits (⚠ new limits below). Not a holding or subsidiary company, a section 8 company, or one under a special Act [SM 9–10] |
| Control | **Subsidiary** s.2(87): the holding company **controls the composition of the Board**, OR controls **more than 50%** (SM: "one-half") of total voting power. *So 35% holding with the power to appoint the majority of directors = subsidiary (Jun'24 MCQ = SM MCQ 14).* · **Associate** s.2(6): **significant influence**, i.e. control of at least **20%** of share capital or of business decisions; includes a JV [SM 10–11] |
| Listing | **Listed** s.2(52): any securities listed. **Not counted as listed:** companies listing only privately placed NCDs or non-convertible redeemable preference shares, and public companies whose equity is listed only abroad [SM 10–11] |
| Others | **Government company** s.2(45): at least **51%** held by CG and/or SG(s), and its subsidiaries · **Foreign company** s.2(42) (part 10) · **Dormant** (s.455): formed for a future project or to hold an asset or IP, with **no significant accounting transaction** in the last **2 FYs**; applies to the ROC · **Nidhi** (s.406): mutual benefit; deposits from and loans to members only · **PFI** s.2(72): LIC, IDFC, UTI's specified company, notified institutions · **Section 8** (part 9) · **JV** (or a contractual JV without a company) · **Sectoral**: banking, insurance, electricity follow both the Act and their sector law · NBFC [SM 11–13] |

**PRIVATE vs PUBLIC (SM table)**

| Point | Private | Public |
|---|---|---|
| members | min 2, max 200 | min 7, no max |
| directors | min 2, max 15 | min 3, max 15 (more by special resolution) |
| public money | cannot raise | can raise |
| share transfer | restricted | free |
| name ends | "Pvt. Ltd." | "Ltd." |

[SM 9]

**Members below the minimum (s.3A):** if a company carries on business for more than **6 months** below the minimum, every member who knows it is **severally liable for all debts** contracted in that period. [SM 9]

**Large partnership (s.464, Rule 10):** an association of more than **50** persons for gain must register as a company (except HUFs and professionals under special Acts). Otherwise it is an **illegal association**: fine up to **₹1 lakh**, personal liability, no legal existence. [SM 13]

**Public sector:** Government departments, statutory corporations, Government companies. **Joint sector** = Government holding **26–50%**. [SM 6]

**DEC'26 SUPPLEMENTARY: SMALL COMPANY · COMPANIES (SPECIFICATION OF DEFINITION DETAILS) AMENDMENT RULES, 2025 · FROM 1 DEC 2025 · ICMAI "EXAMINATION POINT"**

Small company = paid-up capital up to **₹10 crore** and turnover up to **₹100 crore**, with the usual exclusions (holding and subsidiary companies, section 8 companies, special-Act companies). **The SM's ₹4 crore / ₹40 crore are superseded.** [Supp Dec'26 p.2] [SM 10]

## 3 One Person Company (OPC) · Dec'24 Q2(a)

**FEATURES AND RULES**

- **One member**, a **natural person, Indian citizen**. It may be limited by shares, by guarantee, or unlimited. [SM 8]
- A **nominee** named in the memorandum becomes the member on the subscriber's **death or incapacity**. The nominee's **prior written consent** is filed with the ROC at incorporation. [SM 8–16]
- The nominee **may withdraw consent**. The member may **change the nominee** at any time by notice to the company, which tells the ROC. Changing the nominee is **not an alteration of the memorandum**. [SM 16]
- A person may not form **more than one OPC** or be a nominee in more than one. A person who becomes a member of a second OPC as a nominee must comply within **180 days**. [SM 16–17]
- **No minor** may be a member or nominee, or hold shares with beneficial interest. [SM 16]
- No **section 8** conversion; no **NBFI activity**, including investing in securities of a body corporate. [SM 16]
- At least **1** director, up to **15**. **No AGM**; FS signed by **one director**; **no cash flow statement**. "(One Person Company)" appears below its name. [SM 8–19]
- **Penalty** for breaking these rules: up to **₹10,000**, plus up to **₹1,000 a day**. [SM 17]

**⚠ THE SM MIXES OLD AND NEW OPC RULES (2021 AMENDMENT)**

On SM 8 the member and nominee must be "Indian citizen **and resident**", but on SM 17 the rule says Indian citizen "**whether resident in India or otherwise**". The 2021 amendment **removed the residency condition**, so **write the SM 17 version**. [SM 8–17]

SM 16(i) still says an OPC cannot convert voluntarily for **2 years** unless paid-up capital exceeds **₹50 lakh** or turnover exceeds **₹2 crore**. The same 2021 amendment **removed that lock-in and the forced conversion**; an OPC may now convert at any time. Write the SM figure and add the 2021 change. [SM 16]

**Not in the SM, but needed for Dec'24 Q2(a):** when the nominee withdraws, the member must **nominate another person within 15 days** of the withdrawal notice, with the new nominee's consent. The company then informs the ROC.

## 4 Incorporation, commencement of business, effect of registration

**WHO MAY FORM (s.3) · FILING (s.7)**

- **7** or more persons for a public company; **2** or more for a private company; **1** for an OPC. [SM 14]
- **File with the ROC:** MOA and AOA signed by all subscribers · **declaration by a professional** (advocate, CA, CMA or CS in practice) and by a director, manager or secretary named in the articles that the Act has been complied with · **declaration by each subscriber and first director**: not convicted, not guilty of fraud or misfeasance in the last **5 years**, documents true · correspondence address · particulars and ID proof of subscribers and first directors (with DIN), their other interests and **consent**. [SM 14–15]
- The ROC registers and issues the **certificate of incorporation** (SM MCQ 9) with the **CIN**. Copies are kept at the RO till dissolution. False information → **s.447** (fraud). [SM 15]
- **SPICe+ (INC-32)** with **e-MOA (INC-33)**, **e-AOA (INC-34)** and **AGILE-PRO-S (INC-35)**: name, incorporation, DIN, PAN, TAN, EPFO, ESIC, bank account, GSTIN, professional tax. **RUN** is now only for changing an existing name. A **Central Scrutiny Centre** checks STP e-forms (from 23 Mar 2021). [SM 15–16]

**COMMENCEMENT (s.10A) · EFFECT (s.9, s.10)**

- A company with share capital incorporated after the 2019 amendment may not start business or borrow until (a) a director files **INC-20A** within **180 days** of incorporation (verified by a CS, CA or CMA in practice) declaring that every subscriber has paid for his shares, and (b) it has verified its RO in **INC-22**. [SM 18]
- **Default:** company **₹50,000**; each officer **₹1,000 a day**, up to **₹1 lakh**. Without INC-20A in 180 days, the ROC may **strike off** the name. [SM 18]
- **Effect of registration:** a **body corporate** with perpetual succession, able to hold property, contract and sue in its own name. The **certificate is conclusive evidence** of incorporation. [SM 17]
- **s.10:** the MOA and AOA bind the company and members as if **signed by each member** (money due under them is a debt). They are a contract between the **company and members** and among **members inter se** (*Wood v. Odessa Waterworks*), but **not with outsiders**. [SM 17]
- **s.6:** the Act **overrides** the MOA, AOA, agreements and resolutions; anything inconsistent is void. [SM 20]

## 5 Registered office (s.12, s.13(4)): three past MCQs

| Move | What is needed |
|---|---|
| within the same city, town or village | **Board resolution**; notice to the ROC within **15 days** (Dec'24 MCQ = SM MCQ 11) [SM 19] |
| outside local limits, same ROC | **special resolution** + notice to the ROC [SM 19] |
| to another ROC **in the same State** | special resolution + confirmation by the **Regional Director** (Dec'23 MCQ). The RD communicates within **30 days**; the company files it within **60 days**; the new ROC certifies within **30 days**. The certificate is conclusive; the change takes effect from its date [SM 19] |
| to **another State** | alter the memorandum by **special resolution + Central Government approval** (Jun'23 MCQ; MCQ bank 96). The CG decides within **60 days**, checking the creditors' consent or provision for debts. File the order with the ROC of each State; the new State's ROC issues a fresh certificate [SM 22–23] |

**Other s.12 rules:** an RO from the **15th day** of incorporation; **verification within 30 days (INC-22)**. Name and RO address **painted outside every office**, in local characters too. Name, RO, **CIN**, phone, e-mail and website on **letters, bills and notices**. **Former names** of the last **2 years** shown too. Default: **₹1,000 a day**, up to **₹1 lakh**. [SM 18–20]

## 6 Memorandum, name and alteration of the memorandum (s.4, 13, 16)

### CONTENTS OF THE MOA (s.4)

1. **Name** ending "Limited" or "Private Limited"
2. **State** of the registered office
3. **Objects**. A company whose activities change must change its name to match within **6 months**
4. **Liability**: limited by shares (unpaid amount) or guarantee (the amount, payable while a member or within **1 year** after ceasing)
5. **Capital**: amount and division; each subscriber takes at least **one share**
6. **OPC:** the nominee's name

The memorandum is a **public document** (**s.399**; MCQ bank 247): anyone contracting with the company is presumed to know it. [SM 20–21]

### NAME RULES

- Not identical or too similar to an existing company's name; not an offence; not undesirable in the CG's view; nothing suggesting Government patronage without CG approval. [SM 21]
- **Reservation: 20 days** for a new company, **60 days** for a change of name. Extension for a new company: **40 days** (₹1,000), **60 days** (₹2,000 / ₹3,000). [SM 21–22]
- **Wrong information:** before incorporation, name cancelled and penalty up to **₹1 lakh**. After incorporation, the ROC may order a change within **3 months** by ordinary resolution, strike off, or petition for winding up. [SM 21]
- **s.16:** the CG may direct rectification of a name too like an existing company's or a registered trade mark within **3 months** (ordinary resolution); notice to the ROC within **15 days**. [SM 23]

**Altering the memorandum (s.13):** by **special resolution** · **name change** needs CG approval, except adding or deleting "Private" on conversion. Not allowed if the company is in default of filings or deposit/debenture repayment. Effective on the **fresh certificate** · **objects change** while prospectus money is unused: special resolution **by postal ballot**, published in one English and one vernacular newspaper and on the website, with an **exit offer to dissenting shareholders** under SEBI rules. The ROC registers it within **30 days** · no alteration has effect until **registered** · a guarantee company without share capital cannot give a non-member a share of profits. [SM 22–23]

## 7 Articles and the three doctrines · Jun'24 Q5(b), Jun'26 MCQ case

### ARTICLES (s.5, 14, 15, 17)

- The **bye-laws** for management. They may contain **entrenchment** (provisions alterable only on conditions stricter than a special resolution), adopted on formation or later: **all members** agreeing in a private company, a **special resolution** in a public one. Notice to the ROC. [SM 23–24]
- **Model articles** apply to the extent not excluded or modified. [SM 24]
- **Alteration (s.14):** by **special resolution** (SM MCQ 94), including conversions. Filed with the ROC within **15 days** with the altered articles; once registered, valid as if original. [SM 24]
- **s.15:** every copy must show alterations; penalty **₹1,000 per copy**. **s.17:** copies of the MOA, AOA and s.117 resolutions to members within **7 days** of request; default **₹1,000 a day or ₹1 lakh, whichever is less**. [SM 24–25]

### THE THREE DOCTRINES

- **Constructive notice:** the MOA and AOA are **public documents** (s.399), so an outsider is **deemed to know their contents**. He deals incompatibly at his peril; e.g. if the articles require two directors to sign a bill and only one signed, he cannot claim. It operates **only against the outsider**, not the company. [SM 25]
- **Indoor management** (*Royal British Bank v. Turquand*): an outsider may assume the **internal formalities have been complied with**. In Turquand, the bond was valid even though the authorising resolution had never been passed. It is the **limit on constructive notice**. *Jun'26: a bank lending without knowing that Board approval was missing → the company is liable (B).* [SM 25]
- **Ultra vires:** an act **beyond the objects** in the memorandum is void. An act beyond the **Board's** powers but within the company's may be **ratified** by the company, but an act ultra vires the **company cannot be ratified even by all members**. [SM 18]

**⚠ EXCEPTIONS TO INDOOR MANAGEMENT: THE SM GIVES ONE, AN ANSWER NEEDS MORE**

The SM's exception: no protection for information the outsider could reasonably have found with little effort. [SM 25] **The standard exceptions from case law (not in the SM):** (1) the outsider **knew** of the irregularity; (2) **suspicion** or negligence: circumstances should have put him on inquiry; (3) **forgery**: a forged document is void; (4) an act **outside the officer's apparent authority**; (5) the act is **void or illegal** in itself.

## 8 Conversions: public ↔ private, any class (s.14, s.18), LLP ↔ company (s.366) · Dec'23 Q4(b), Jun'26 Q4(a)

**PRIVATE → PUBLIC (JUN'26 Q4(a))**

1. pass a **special resolution** altering the articles to **remove the s.2(68) restrictions** (share transfer, 200 members, public invitation) [SM 9]
2. it **ceases to be private from the date of alteration**
3. file the alteration and printed altered articles with the ROC within **15 days**
4. delete "Private" from the name (no CG approval needed for that)
5. meet public company rules: at least **7 members, 3 directors**; the ROC issues a fresh certificate (s.18)

[SM 8–24]

**PUBLIC → PRIVATE (DEC'23 Q4(b))**

1. **special resolution** altering the articles to **add the s.2(68) restrictions**; binding on dissenters if bona fide and in the company's interest
2. members within **200** [SM 9] (count as in part 2: joint holders = 1; current and ex-employee members excluded)
3. **approval** on application (⚠ below)
4. file the alteration and approval order with the ROC within **15 days**; add "Private" to the name

[SM 8–24]

**⚠ "APPROVAL OF THE TRIBUNAL" OR "OF THE CENTRAL GOVERNMENT"? THE SM SAYS BOTH**

SM 13 says the **Tribunal**; SM 24 says the **Central Government**. The 2019 amendment moved this to the **Central Government** (exercised by the **Regional Director**). **Write the Central Government (Regional Director).** [SM 13–24]

**s.18 (any class to another):** alter the MOA and AOA, apply to the ROC, who **closes the former registration** and issues a **fresh certificate**. **Debts, liabilities, obligations and contracts** from before conversion are **unaffected**. [SM 26] The SM lists the possible conversions: private ↔ public, OPC → private/public, private → OPC, section 8 → other, LLP → company, private or unlisted public → LLP. [SM 30]

**LLP (OR FIRM) → COMPANY, s.366 + AUTHORISED TO REGISTER RULES (MQP Q4(b))**

1. partners' meeting: name (same name + "Ltd" or "Pvt Ltd"; valid **60 days**) and authority to act [SM 30]
2. **DSC and DIN** for the future directors [SM 31]
3. **advertisement** in a local and a national newspaper; **NOC** from the ROC where the LLP is registered [SM 30]
4. file **URC-1** with: a list of partners (as on a day not more than **6 clear days** before applying) and their shares (cash / non-cash); first directors' particulars and consent; the partnership deed and registration certificate (for a firm); **consent or NOC of all secured creditors**; **written consent of the majority** of members at a general meeting [SM 31–33]
5. at least **2 members**; with fewer than **7** it registers as a **private company** (the old minimum of 7 partners was relaxed in 2017) [SM 30–31]

**COMPANY → LLP (LLP Act s.58, Schedules III–IV)**

- Only a **private company** or an **unlisted public company**. [SM 31]
- Board resolution; **written consent of all shareholders**; name approval in **RUN-LLP** (with the Board resolution). [SM 31–32]
- LLP agreement: name, partners and designated partners, contribution, profit share, rights and duties, business, rules. Filed in **Form 3** within **30 days**. [SM 32]
- Apply in **Form 18** with a statement of shareholders and an **auditor-certified statement of assets and liabilities**. [SM 32]
- *SM MCQ 16: after converting into an LLP, intimation to the ROC within **15 days**.*

## 9 Section 8 (not-for-profit) companies · Dec'25 Q4(b), ICMAI PTP case

### WHEN THE CG LICENSES IT

a. its **objects**: commerce, art, science, sports, education, research, social welfare, religion, charity, environment, or similar
b. it **applies its profits or income only to those objects**
c. it **prohibits dividends** to members (SM MCQ 12; MCQ bank 301)

The CG then licenses it to register **without "Limited" / "Private Limited"** in its name. Apply in **INC-12** with the MOA (**INC-13**), a declaration (**INC-14**) and **3-year** income and expenditure projections. An existing company may also apply (INC-12, with past FS and audit reports). [SM 26–27]

### CONSEQUENCES

- It has all the privileges and obligations of a limited company; a **firm may be a member**. [SM 26]
- It may **alter its MOA or AOA only with prior CG approval**; it converts into another kind only on prescribed conditions. [SM 26]
- **Licence revoked** if its affairs are run fraudulently, against its objects, or against the public interest. It then adds "Ltd"/"Pvt Ltd", and may be **wound up** or **amalgamated** with another section 8 company. [SM 27]
- **Surplus assets** on winding up go to another section 8 company with similar objects, or are sold with the proceeds credited to the **Rehabilitation and Insolvency Fund** (s.269). It may **merge only with section 8 companies** with similar objects. [SM 27]
- **Penalty:** company **₹10 lakh to ₹1 crore**; directors and officers **₹25,000 to ₹25 lakh**; if fraud, **s.447**. [SM 27]
- **Dec'25 answer in brief:** earning only "marginal profits" does **not** make it non-profit. It needs the **three conditions in its MOA and a CG licence**, and it may operate pan-India from its RO. Profits are allowed, but **never distributed**.

## 10 Foreign companies (Chapter XXII, s.379–393)

### DEFINITION AND THE MCQs

- **s.2(42):** a company or body corporate **incorporated outside India** that (a) has a **place of business in India**, itself or through an agent, physically or electronically, and (b) conducts any business activity in India in any other manner. [SM 11–27]
- **MCQ key (SM MCQ 5 = Jun'23):** "**either (a) or (b)**". A US company doing business only in the USA is **not** a foreign company, but becomes one once it starts business in India (**both**: SM MCQ 92 = Dec'25). An Indian company 100% owned by a UK company is an **Indian company** (SM MCQ 13). Chapter **XXII** (SM MCQ 17).
- **s.379:** if Indian citizens or Indian companies hold at least **50%** of its paid-up capital, it complies with Chapter XXII **as if incorporated in India**. [SM 28]
- Inspection and investigation (Chapter XIV) apply. It may **merge** with an Indian company (or vice versa) with **RBI's prior approval** (s.234(2)). If it stops business in India, it may be wound up as an **unregistered company** (s.376). [SM 27–28]

### COMPLIANCE

- **s.380:** within **30 days** of setting up a place of business, file: its charter or MOA/AOA (with an English translation), its principal office address, directors and secretary, **persons resident in India authorised to accept service**, its principal place of business in India, earlier openings and closings, and a declaration that no director or representative is convicted or debarred. Alterations within **30 days**. [SM 28]
- **s.381:** every **calendar year**, a balance sheet and P&L (English translation) and a list of Indian places of business, filed with the ROC. [SM 28–29]
- **s.382:** display its name and **country of incorporation** outside every office (in English and the local language) and on letters and notices; state limited liability where it applies. [SM 29]
- **s.383:** service on the person registered under s.380, by post or electronically. Debentures (s.71), annual return (s.92), books in India (s.128) and charges (Chapter VI) also apply. [SM 29–30]

## 11 Model answers

**MODEL ANSWER 1 · PUBLIC → PRIVATE: COUNTING THE 200 MEMBERS (DEC'23 Q4(b)) · 7 MARKS**

**Facts:** KFR Ltd (public) has 230 members: directors and relatives 50; employees 15; ex-employees who got shares while employed 10; 5 couples holding jointly (10 persons); others 145. The Board wants to convert it into a private company. Must the number of members be reduced?

**Provision:** a private company's articles limit members to **200** (s.2(68)). **Joint holders count as one member**. **Employees**, and **ex-employees who became members while employed**, are **not counted**. Conversion needs a **special resolution** altering the articles and **Central Government (RD) approval**, with the order filed within 15 days (s.14). [SM 8–24]

| Group | Persons | Counted | Why |
|---|---|---|---|
| directors and relatives | 50 | 50 | counted like any member |
| employees | 15 | 0 | excluded |
| ex-employees (shares allotted while employed) | 10 | 0 | excluded |
| 5 joint-holding couples | 10 | 5 | joint holders = one member |
| others | 145 | 145 | counted |
| **total** | **230** | **200** | **exactly at the limit** |

**Conclusion:** the members for the s.2(68) count are **200**, which is **within the limit**. **No reduction is needed.** KFR may convert by special resolution, with the altered articles adding the private-company restrictions, CG (RD) approval, filing with the ROC, and "Private" added to its name.

**MODEL ANSWER 2 · OPC NOMINEE CASE (DEC'24 Q2(a)) · 7 MARKS**

**Facts:** Gautam formed an OPC with his brother Rohit as nominee. Rohit moved permanently to Dubai and withdrew his nomination. (i) What must Gautam do, and by when? (ii) Can he nominate his minor son? (iii) What if he fails to nominate?

1. **Law:** an OPC's memorandum must name a **nominee** who becomes the member on the subscriber's death or incapacity; the nominee gives written consent and **may withdraw it**. The member may change the nominee by notice to the company, which informs the ROC; this is not an alteration of the memorandum. The member and nominee must be **natural persons and Indian citizens**; residency is **no longer required** (SM 17, 2021 rules). [SM 8–17]
2. **(i)** Rohit's withdrawal is valid. Gautam must **nominate a new person, with that person's written consent, within 15 days** of the withdrawal notice, and give notice to the OPC, which informs the ROC. (Moving to Dubai alone would not have disqualified Rohit after 2021, as long as he is an Indian citizen.)
3. **(ii) No.** A **minor cannot be a member or nominee** of an OPC. [SM 16]
4. **(iii)** The OPC and every officer in default are liable to a penalty of up to **₹10,000**, plus up to **₹1,000 a day** while the default continues. [SM 17]

**MODEL ANSWER 3 · LLP CONVERTING INTO A COMPANY (ICMAI MQP Q4(b)) · 7 MARKS**

Under **s.366** and the Companies (Authorised to Register) Rules, an LLP (or firm) may register as a company. Steps: (1) partners resolve on the **name** (the LLP name plus "Ltd"/"Pvt Ltd", valid 60 days) and authorise a partner; (2) obtain **DSC/DIN** for the future directors; (3) **advertise** in a local and a national newspaper and obtain an **NOC** from the ROC; (4) file **URC-1** with the list of partners and shares (as on a day not more than 6 clear days before), the first directors' particulars and consent, the LLP or partnership documents, **consent or NOC of all secured creditors**, and **majority consent** of members; (5) at least **2** members; with fewer than 7 it becomes a **private company**. **Effect:** a new body corporate; the incorporation provisions of Chapter II apply mutatis mutandis. [SM 30–33]

## SM exercise MCQs on 1.1, with answers (SM 158–172; ★ = asked in an exam)

| | | | |
|---|---|---|---|
| 1 minimum members, public company | **7** | 10 professional declaration at incorporation by | **practising CS, CA or CMA: any** |
| 2 Govt company: 51% held by | **CG, SG or both: any** | 11 RO moved within city ★ | **Board resolution** |
| 3 "limited" means limited | **liability of members** | 12 section 8 companies cannot | **distribute dividend** |
| 4 share transfer restricted in | **private company** | 13 Indian co, 100% held by a UK co | **an Indian company** |
| 5 foreign company: abroad and ★ | **either place of business or business in India** | 14 35% held + majority of Board ★ | **subsidiary** |
| 6 no significant accounting transaction | **dormant company** | 15 guarantee company is similar to | **LLP** |
| 7 LIC is | **statutory corporation and PFI** | 16 company → LLP: intimate ROC within | **15 days** |
| 8 those who sign the MOA | **subscribers to MOA** | 17 chapter on foreign companies | **XXII** |
| 9 certificate of incorporation issued by | **ROC** | 92 US company doing business in US ★ | **not foreign now; foreign once in India** |
| 93 sectoral company complies with | **Companies Act + sector law** | 94 articles altered by | **special resolution** |
| bank 96: RO to another State ★ | **special resolution + CG** | bank 243 / 246 / 248 | **OPC max 15 directors / INC-22 / INC-12** |

## R Revision: every number in 1.1

| Rule | Number |
|---|---|
| Act: chapters / sections / schedules | 29 / 470 / 7 |
| members: OPC / private / public | 1 / 2–200 / 7+ |
| business below minimum members for | > 6 months |
| joint sector Govt holding | 26–50% |
| Government company | ≥ 51% |
| subsidiary voting power | > 50% |
| associate: significant influence | ≥ 20% |
| dormant: no significant transaction for | 2 FYs |
| small company (Dec'26 supp.) | ₹10 cr / ₹100 cr |
| large partnership limit / fine | 50 / ₹1 lakh |
| OPC: nominee in more than one / comply within | no / 180 days |
| OPC: SM conversion lock / capital / turnover ⚠ | 2 yrs / ₹50 lakh / ₹2 cr |
| OPC penalty | ₹10,000 + ₹1,000/day |
| subscriber declaration look-back | 5 years |
| INC-20A within / penalty | 180 days / ₹50,000 |
| officer: per day / max | ₹1,000 / ₹1 lakh |

| Rule | Number |
|---|---|
| RO from the … day / verification INC-22 | 15th / 30 days |
| RO change notice to ROC | 15 days |
| RD confirms / company files / ROC certifies | 30 / 60 / 30 days |
| former names shown for | 2 years |
| s.12 default | ₹1,000/day, max ₹1 lakh |
| State change: CG decides within | 60 days |
| name to match changed activities within | 6 months |
| name reserved: new / existing | 20 / 60 days |
| extension 40 / 60 days fee | ₹1,000 / ₹2,000 or ₹3,000 |
| wrong name info: penalty / change within | ₹1 lakh / 3 months |
| objects change registered within | 30 days |
| articles alteration filed within | 15 days |
| s.15 / s.17 penalty | ₹1,000 per copy / per day (max ₹1 lakh) |
| s.8 penalty: company / officers | ₹10 lakh–₹1 cr / ₹25,000–₹25 lakh |
| s.8 projections for | 3 years |
| s.379 Indian holding / s.380 filing | ≥ 50% / 30 days |
| LLP → company: members / list date | ≥ 2 (<7 private) / 6 clear days |

# 1.2 · Investments, Loans and Deposits

P13 · Module 1 · s.73–76A, 186, 187 + debentures

SM pp. 34–43 (10 pages). 39 marks in 7 papers, with a long question in 4, **twice as a balance-sheet calculation**. Nothing in Jun'26, so it is due.

| Paper | What was asked | Marks |
|---|---|---|
| Dec'23 | Q2(a) the prohibition on accepting **deposits from the public** (s.73) | 7 |
| Jun'24 | Q8(a) must investments be held in the **company's own name**? (s.187) | 7 |
| Dec'24 | MCQ: meaning of "loan" | 2 |
| Jun'25 | Q2(a) s.187 again, with its exemptions · Q4(a) **inter-corporate loan case** from a balance sheet: s.186 limit and interest rate | 7 + 7 |
| Dec'25 | MCQ: who can be a debenture trustee · Q2(b) **public deposits case** from a balance sheet: eligibility and limits (repeated in ICMAI's MQP) | 2 + 7 |

**HOW IT IS EXAMINED · DEC'26 PREDICTION**

- **Number cases:** you get a balance sheet; compute the **s.186 limit** or the **deposit limits**. Know **what counts**: paid-up capital, **free reserves** (P&L, general reserve) and securities premium. **Revaluation reserve is not free**.
- Theory: **s.187 own-name investments** (2×), **s.73 deposits**.
- **Prediction:** Tier A, **7–9 marks**. (1) deposits case (MQP) · (2) inter-corporate loan above the s.186 limit · (3) s.185 loans to directors, never asked long (see 1.5 part 9).

**MAP**

1. Loans and investments by a company (s.186) ★★★
2. Investments in own name (s.187) ★★
3. Deposits: s.73, rules, s.74–76A ★★★
4. Debentures ★ (MCQs)
5. Model answers (both number cases) · MCQs · numbers

Loans to directors (s.185) are in 1.5 part 9.

## 1 Loans, guarantees, security and investments by a company (s.186)

**WHAT IT IS** Lending to, guaranteeing for, or investing in other bodies is the **Board's** power (s.179). s.186 sets a **ceiling**: above it, a **special resolution** is needed. It also fixes the **minimum interest rate**. A guarantee is treated like a loan, because the company may have to pay. [SM 34]

**LAYERS**
invest through **not more than two layers** of investment companies (except buying a foreign company with more layers abroad, or a subsidiary legally required) [SM 34]

→

**THE LIMIT**
loans + guarantees + security + investments ≤ **60%** of (paid-up capital + free reserves + securities premium) **or 100%** of (free reserves + securities premium), **whichever is more** [SM 34]

→

**ABOVE THE LIMIT**
prior **special resolution** in general meeting. Not needed for a holding company's dealings with its **wholly owned subsidiary or JV** [SM 34–35]

→

**ALWAYS**
Board resolution with **consent of all directors present**, plus **PFI approval** if a PFI term loan subsists (not needed if within the limit and no default) [SM 35]

**OTHER RULES**

- **Interest**: never **below the prevailing yield** of the **1-, 3-, 5- or 10-year Government security closest to the tenor** of the loan. [SM 35]
- A company **in default on deposits** (or interest) may give **no loan, guarantee, security or investment** while the default lasts. [SM 35]
- **Disclose** full particulars and the **purpose** in the financial statements. [SM 35]
- Keep a **register** (MBP-2) at the RO; members inspect and take extracts free, and get copies for a fee. [SM 35]
- A SEBI-registered intermediary (s.12, SEBI Act) of a prescribed class may not take inter-corporate loans or deposits above the prescribed limit. [SM 35]

**EXEMPT (all of s.186 except the layers rule)**

- **Loans, guarantees, security** in the ordinary course by a **banking, insurance or housing finance company**, or a company financing industry or providing infrastructure. [SM 35]
- **Investments** by an **investment company**, an **NBFC**, or a company whose principal business is acquiring securities · **rights issue** subscriptions · shares under s.62(1)(a). [SM 35]
- **Penalty:** company **₹25,000 to ₹25 lakh**; each officer up to **2 years** in jail and a fine of **₹25,000 to ₹1 lakh**. [SM 35]

**⚠ MCQ BANK vs SM**
MCQ bank Q86 "not more than ___ layer of investment companies" gives **1**, but the SM text says **two layers**. Trust the SM. [SM 34]

## 2 Investments to be held in the company's own name (s.187) · Jun'24 Q8(a), Jun'25 Q2(a)

**THE RULE**

- **All investments** in any property, security or other asset are made and held **in the company's own name**. [SM 36]
- **Proviso:** shares in a **subsidiary** may be held in the name of **nominees** where needed to keep the subsidiary's membership above the **statutory minimum**. [SM 36]
- **SM example:** ABC holds 100% of XYZ Pvt Ltd, which needs 2 members. ABC may put **one** share in a nominee's name, but only one. [SM 36]
- Shares or securities **not held in its own name** are entered in a **register** (MBP-3), open to members and debenture holders **free** during business hours. [SM 36]

**EXEMPTIONS: THE COMPANY MAY STILL …**

1. deposit shares or securities with a **bank to collect dividend or interest**
2. deposit with, transfer to, or hold in the name of **SBI or a scheduled bank** (its bankers) to **facilitate transfer**
3. deposit or transfer them as **security for a loan**
4. hold them in the name of a **depository** as beneficial owner (demat)

[SM 36]

## 3 Deposits (s.73–76A + Acceptance of Deposits Rules) · Dec'23 Q2(a), Dec'25 Q2(b)

**WHAT IT IS** "**Deposit**" (s.2(31)) includes **any receipt of money by way of deposit or loan or in any other form**, except categories prescribed with the RBI. The Act allows only two routes: **from members** (s.73(2)) and **from the public** by an **eligible company** (s.76). Banks, NBFCs and companies the CG specifies are outside. [SM 36]

### ROUTE 1: FROM MEMBERS, s.73(2)

By **resolution in general meeting**, on these conditions:

1. a **circular** to members showing the financial position, **credit rating**, number of depositors and dues on past deposits
2. the circular **filed with the ROC 30 days** before it is issued
3. by **30 April** each year, at least **20%** of deposits maturing in the year put in a **Deposit Repayment Reserve Account** in a scheduled bank
4. a certificate of **no default** on past deposits (or the default made good and **5 years** passed)
5. **security** if any; unsecured or partly secured deposits must be called "**unsecured deposits**" everywhere

[SM 36–37]

### ROUTE 2: FROM THE PUBLIC, s.76 · "ELIGIBLE COMPANY"

- A **public company** with **net worth ≥ ₹100 crore OR turnover ≥ ₹500 crore**, which has passed a **special resolution**. [SM 38–41]
- It needs a **credit rating** from a recognised agency, **every year** of the deposit tenure. [SM 41]
- **Secured deposits:** a charge on assets, not less than the deposits, within **30 days** of accepting. [SM 41]
- Circular in the form of an advertisement: **DPT-1** (MCQ bank 234).

**⚠ "AND" OR "OR"?**
SM 38 says net worth ₹100 cr "**and**" turnover ₹500 cr; SM 41 (s.76) says "**or**". The Rules say **or**. Write **or**. [SM 38–41]

### Limits and terms (Rule 3) [SM 37–38]

| Rule | Limit |
|---|---|
| **Tenure** | not repayable on demand; at least **6 months**, at most **36 months** [SM 37] |
| **Short-term** (under 6 months) | up to **10%** of (paid-up capital + free reserves), repayable **not earlier than 3 months** [SM 37] |
| Members' deposits (s.73(2) company) | all outstanding deposits ≤ **35%** of (paid-up capital + reserves + securities premium) [SM 37–38] |
| **Eligible company**, from members | ≤ **10%** of (paid-up capital + free reserves) [SM 38] |
| **Eligible company**, other (public) deposits | ≤ **25%** of (paid-up capital + free reserves + securities premium) [SM 38] |
| Government company (s.76) | ≤ **35%** of (paid-up capital + free reserves + securities premium) [SM 38] |
| Interest and brokerage | not above the **RBI's maximum for NBFC deposits** (SM MCQ 23) · joint names at most **3** · no term changed to the depositor's disadvantage after issue [SM 38] |

⚠ For the members' 10% limit, the SM's base is paid-up capital + free reserves. A later amendment to the Rules also adds securities premium. In a calculation, show the SM figure and note the other.

**SECURITY AND TRUSTEES (Rules 6–9)**

- Secured deposits: a **charge** (not a pledge) on specific movable or immovable property, for at least the amount **not covered by deposit insurance**, in favour of a **trustee for depositors**. [SM 38]
- Trustee appointed and **deposit trust deed (DPT-2)** signed at least **7 days** before the circular. The trustee may not be a director, KMP, employee or depositor, indebted to the company, financially related to it, a guarantor, or a relative of these. [SM 38–39]
- He is removed before his term only with **consent of all directors present** (with at least one ID where IDs are required). [SM 39]
- **Duties:** check the security plus insurance covers the deposits; check the circular; prevent breaches; seek remedies; call meetings; supervise security; act when it becomes enforceable; protect depositors. [SM 39]
- **Depositors' meeting:** on a requisition by **one-tenth in value**, or on a default or any event affecting depositors. [SM 39]

**REPAYMENT, REGISTERS, PENALTIES**

- **Default:** the depositor may apply to the **Tribunal** for payment and damages. The **DRRA** is used only to repay deposits; its balance never falls below **15%** of deposits maturing in the current and next financial year. [SM 37–40]
- **Register of deposits** at the RO (name, PAN, nominee, amounts, dates, rate, insurance, security); entries within **7 days** of the receipt; kept for **8 years** (SM MCQ 20: mandatory, particulars as per the Rules). [SM 40–41]
- **s.74** (deposits from before the Act): statement to the ROC within **3 months**; repay within **3 years** or by maturity, whichever is earlier (the Tribunal may extend). Fine **₹1 crore to ₹10 crore**; officers up to **7 years** in jail and/or **₹25 lakh to ₹2 crore**. [SM 40]
- **s.75 fraud:** officers who accepted deposits to defraud are **personally liable without limit**; any person or group may sue. [SM 41]
- **s.76A** (breach of s.73 or s.76): company fine of at least **₹1 crore or twice the deposit, whichever is lower**; officers up to **7 years** in jail and a fine of **₹25 lakh to ₹2 crore**; if wilful, s.447. [SM 41–42]

## 4 Debentures (MCQ material)

**s.2(30):** "debenture" includes **debenture stock, bonds or any other instrument evidencing a debt**, whether or not it creates a charge on assets. [SM 42]

| Type | Meaning |
|---|---|
| redeemable / irredeemable | fixed redemption date / none (perpetual: repaid on liquidation or by notice) [SM 42] |
| convertible / non-convertible / optionally convertible | must convert into equity / stays debt till redemption / the holder chooses [SM 42–43] |
| fully / partly convertible | all into equity / part converts, the rest redeemed. *SM example: a ₹100 debenture → 10 shares of ₹10 (fully), or ₹50 into 5 shares with ₹50 repaid after 10 years (partly)* [SM 42–43] |
| secured / unsecured | a charge on assets (mortgage) / naked. A **public issue maturing beyond 18 months must be secured**, with a **SEBI-registered debenture trustee** holding the security (SM MCQs 18, 21; Dec'25 MCQ) [SM 43] |
| fixed / floating rate · zero coupon | a fixed rate / one linked to a benchmark · no interest: issued at a **discount** ("discounted bonds"; "**deep discount**" if long-dated), sometimes with a warrant [SM 43] |

## 5 Model answers: the two number cases

**MODEL ANSWER 1 · INTER-CORPORATE LOAN (JUN'25 Q4(a)) · 7 MARKS**

**Facts (₹ lakh):** XYZ Ltd: paid-up capital 40; P&L balance 22; share premium 10; machinery revaluation reserve 11; secured loan from a nationalised bank 35 (11%). ABC Ltd asks for a secured loan of **40** for **40 months**. G-sec yields: 1 yr 6.5%, 2 yrs 6.7%, 3 yrs 6.9%. Can the loan be granted, and at what rate?

| Step | Working |
|---|---|
| Free reserves | P&L balance **22**. The **revaluation reserve (11) is not a free reserve**; leave it out. |
| Limit (a): 60% of (paid-up + free reserves + premium) | 60% × (40 + 22 + 10) = 60% × 72 = **43.2** |
| Limit (b): 100% of (free reserves + premium) | 22 + 10 = **32** |
| s.186 limit = the higher | **43.2 lakh** |
| Proposed loan | 40 ≤ 43.2: **within the limit** (assuming no other loans or investments outstanding), so **no special resolution** is needed |
| Approval | a **Board resolution with the consent of all directors present**. PFI approval is not needed: the loan is within the limit, there is no default, and a nationalised bank is not a PFI |
| Interest rate | not below the G-sec yield **closest to the tenor**. 40 months is nearest the **3-year** security, so **at least 6.9%** |

**Conclusion:** XYZ **can** grant the ₹40 lakh loan by a Board resolution with the consent of all directors present, at an interest rate of **at least 6.9%**, and disclose it in the financial statements and the s.186 register. If its existing loans and investments plus this loan crossed ₹43.2 lakh, a **prior special resolution** would be needed. [SM 34–35]

**MODEL ANSWER 2 · PUBLIC DEPOSITS (DEC'25 Q2(b), ALSO ICMAI MQP Q2(a)) · 7 MARKS**

**Facts (₹ crore):** Pearson Ltd (public, steel pipes): paid-up equity 100; general reserve 20; securities premium 5; term loan from SBI 75; turnover 575. It wants public deposits of 3 to 36 months.

1. **Eligible?** An eligible company is a **public company** with net worth ≥ ₹100 cr **or** turnover ≥ ₹500 cr that passes a **special resolution**. Net worth = 100 + 20 + 5 = **125**; turnover **575**. Both tests are met, so it is **eligible**, subject to a special resolution (filed with the ROC), a **credit rating**, and the circular (DPT-1). [SM 38–41]
2. **Limit for public deposits:** 25% of (paid-up capital + free reserves + securities premium) = 25% × 125 = **₹31.25 crore**. [SM 38]
3. **Less than 6 months?** Yes, up to **10%** of (paid-up capital + free reserves) = 10% × 120 = **₹12 crore**, repayable **not earlier than 3 months**. So the 3-month deposits are fine within ₹12 crore. Maximum tenure **36 months**. [SM 37]
4. **From members (separately):** 10% of (paid-up capital + free reserves) = **₹12 crore** (⚠ ₹12.5 crore if the securities premium is added, as the amended Rules do). [SM 38]
5. **Also:** by 30 April, **20%** of deposits maturing in the year go into the DRRA; interest and brokerage within RBI's NBFC ceilings; a charge within **30 days** if secured. The SBI term loan does not affect eligibility. [SM 37–41]

### SM exercise / MCQ bank on 1.2, with answers

| | | | |
|---|---|---|---|
| 18 secured public-issue debentures: security in favour of | **debenture trustee** | 21 a debenture trustee can be ★ | **any entity registered with SEBI as such** |
| 19 a fully convertible debenture is a | **debt instrument** (bank key) | 22 "loan" in the Companies Act means ★ | **cash credit** (bank key ⚠) |
| 20 register of deposits | **mandatory, with particulars as per the Rules** | 23 brokerage on deposits | **as per RBI** |
| bank 87: interest on deposits guided by | **RBI** | bank 233: trust deed before circular | **7 days** |
| bank 234: advertisement circular in form | **DPT-1** | bank 86: layers of investment companies | **bank key 1 ⚠ SM says two** |

⚠ The SM text has no definition of "loan"; the Dec'24 MCQ answer follows ICMAI's MCQ bank key.

## R Revision: every number in 1.2

| Rule | Number |
|---|---|
| layers of investment companies | 2 |
| s.186 limit | 60% (PUC+FR+SP) or 100% (FR+SP), higher |
| loan interest floor: G-sec tenors | 1, 3, 5, 10 yrs |
| s.186 penalty: company | ₹25,000–₹25 lakh |
| s.186 officer: jail / fine | 2 yrs / ₹25,000–₹1 lakh |
| members' circular filed before issue | 30 days |
| DRRA: deposit by / share of maturing | 30 April / 20% |
| DRRA floor | 15% |
| clean record after default | 5 years |
| eligible company: net worth / turnover | ₹100 cr / ₹500 cr |
| charge for secured public deposits within | 30 days |

| Rule | Number |
|---|---|
| tenure: minimum / maximum | 6 / 36 months |
| short-term: limit / earliest repayment | 10% / 3 months |
| s.73(2) members / Govt company | 35% / 35% |
| eligible company: members / public | 10% / 25% |
| joint depositors, at most | 3 |
| DPT-2 trust deed before circular | 7 days |
| depositors' meeting requisition | one-tenth in value |
| register entries / kept for | 7 days / 8 years |
| s.74: statement / repay within | 3 months / 3 years |
| s.74 / s.76A officer jail | 7 years |
| s.76A company fine | ₹1 cr or 2× deposit, lower |
| public debentures must be secured beyond | 18 months |

# 1.8 · Compromises, Arrangements and Amalgamations P13 · Module 1

· Chapter XV, s.230–240

SM pp. 141–149 (9 pages). 32 marks in 7 papers, **always as a 7-mark half** (5 papers). ICMAI's PTP turned the Jun'23 merger case into a 4-MCQ set.

| Paper | What was asked | Marks |
|---|---|---|
| Jun'23 | Q4(a)(I) **unlisted holding company (70%) merges with its listed subsidiary**: in order? shareholders' approval? dissenters? NCLT order needed? | 4 |
| Dec'23 | Q5(b) **minority squeeze-out** in a reconstruction: price set by the promoters, more than 90% voted for it; can the minority reject? | 7 |
| Dec'24 | Q8(b) **amalgamation by the Central Government** in the public interest (s.237) | 7 |
| Dec'25 | Q3(b) s.237 again: **dissenting shareholders' remedy** on compensation (also ICMAI MQP) | 7 |
| Jun'26 | Q4(b) **compromise and arrangement (s.230)**: procedure, role of the Tribunal, filing | 7 |

**DEC'26 PREDICTION · HOW TO ANSWER**

- Tier A, **7 marks**; an **80%** chance of the 4-MCQ case set (PTP ran one on the Jun'23 facts).
- Likely: (1) **holding + listed subsidiary merger** case, and **when the fast track (s.233) applies** · (2) s.237 (asked twice running, so less likely a third time) · (3) **s.236/minority buy-out**.
- Write procedure questions as a **flow**: application → meetings → approvals → sanction → filing.

**MAP**

1. Meanings · s.230 compromise or arrangement ★★★
2. Tribunal's powers (s.231) · merger (s.232) ★★
3. Fast-track merger (s.233) ★★
4. Cross-border (s.234) · dissenters and minority (s.235, 236, 230(7)) ★★
5. Amalgamation by the CG (s.237) ★★
6. Model answers · MCQs · numbers

# 1 Meanings, and compromise or arrangement (s.230) · Jun'26 Q4(b)

### MEANINGS

- **Compromise**: settling a **dispute** by mutual concessions. No dispute, no compromise; if members give up their rights entirely, it is not a compromise. [SM 141]
- **Arrangement**: very wide. Any reorganisation of share capital (consolidation or division of classes, varying special rights), between classes of shareholders, or between creditors and shareholders (*Investment Corp. of India*). [SM 141]
- **Amalgamation**: two or more companies join into a new one, or one is absorbed into another. The amalgamating company **loses its existence** and its shareholders become shareholders of the amalgamated company. **Not defined** in the Act. [SM 141]

### WHO AND WITH WHOM

- Between the company and its **creditors** (or a class), or its **members** (or a class). [SM 141]
- Application to the **NCLT** by the **company, any creditor, any member, or the liquidator** (jointly too). [SM 141–142]
- The application discloses: the latest financial position and auditor's report, pending investigations, any **reduction of capital**, and any **corporate debt restructuring** consented to by **75% of secured creditors in value** (with a creditors' responsibility statement, safeguards, the auditor's liquidity-test report, RBI CDR guidelines and a **registered valuer's** report). [SM 142]

## The s.230 procedure, step by step [SM 142–144]

**1 · APPLY** to the NCLT, with full disclosure [SM 142]

→

**2 · NCLT ORDERS MEETINGS** of the creditors or members (by class), held as it directs [SM 142]

→

**3 · NOTICE** individually (Form 15.3) with the scheme's effect, valuation, interests, and investigations; on the website; for listed companies to **SEBI and the exchanges**; in newspapers [SM 142–143]

→

**4 · REGULATORS** notice to the CG, income tax, RBI, SEBI, ROC, exchanges, OL, CCI and sector regulators: representations within **30 days**, else none presumed [SM 143]

→

**5 · VOTE** a **majority of persons representing three-fourths in value**, in person, by proxy or postal ballot [SM 144]

→

**6 · SANCTION** the NCLT's order makes it **binding on all**. File with the ROC within **30 days** [SM 144]

- **Who may object:** only persons with at least **10% of the shareholding** or at least **5% of total outstanding debt**. [SM 143]
- The notice includes directors', KMP's and promoters' shareholding and changes in the last **6 months**, approvals received, documents for inspection, and a declaration that the scheme is in the interest of employees, creditors and minority shareholders. [SM 143]
- **The NCLT may dispense with a creditors' meeting** if creditors holding at least **90% in value** consent by affidavit. [SM 144]
- **The NCLT's order provides for:** convertible preference shareholders choosing cash for dividend arrears or equity · protection of any class of creditors · variation of rights under **s.48** · an **exit offer to dissenting shareholders** and other matters. [SM 144]
- The company's **auditor certifies** that the accounting treatment conforms to the accounting standards. [SM 144]
- A **statement of compliance** is filed with the ROC within **210 days**. [SM 144]
- **Takeover offer within a scheme (s.230(11))**: by a member who, with others, holds at least **three-fourths** of the shares, to acquire the rest. For listed companies, under SEBI regulations. [SM 144]
- **s.231:** the NCLT **supervises implementation**, gives directions or modifies the scheme, and may call for reports. If the scheme cannot work and the company cannot pay its debts, it may order **winding up**. [SM 144]

## 2 Merger and amalgamation through the NCLT (s.232)

When the s.230 application is for a **reconstruction, merger or amalgamation** transferring an undertaking, property or liabilities to another company, the NCLT orders meetings and **s.230 applies with necessary modifications**. [SM 145]

### CIRCULATED FOR THE MEETINGS

1. the **draft scheme** adopted by the directors of the merging company
2. confirmation that it has been **filed with the ROC**
3. the directors' report on its effect on each class, KMP, promoters and non-promoters, with the **share exchange ratio** and any valuation difficulties
4. the **expert's valuation report**
5. a **supplementary accounting statement** if the last accounts are more than **6 months** old at the first meeting

[SM 145]

### THE NCLT'S ORDER PROVIDES FOR

- transfer of the undertaking, property and liabilities from the date the parties fix · allotment of shares and debentures · **continuation of pending legal proceedings** [SM 145]
- **dissolution of the transferor without winding up** (SM MCQs 70, 84) · provision for **dissenters** · allotment to non-residents per FDI norms · **transfer of employees** [SM 145–146]
- **Listed transferor, unlisted transferee:** the transferee **stays unlisted until it lists** (SM MCQ 73); shareholders who opt out are **paid** per a predetermined price formula or valuation [SM 146]
- the transferor's **authorised-capital fees are set off** against the transferee's [SM 146]
- the **auditor's certificate** on the accounting treatment (SM MCQ 71) [SM 146]

**After sanction:** property and **liabilities pass** to the transferee (SM MCQ 72: both) and charges may be released · certified order filed with the ROC within **30 days** · the scheme states an **appointed date** and is effective from it, not later · until completion, an **annual statement** certified by a practising CA, CMA or CS is filed with the ROC on compliance. [SM 146]

## 3 Fast-track merger (s.233): no NCLT

### WHO MAY USE IT

- **Two or more small companies** (small company: SM 147; ⚠ now **₹10 cr / ₹100 cr** per the Dec'26 supplementary, see 1.1) [SM 146–147]
- a **holding company and its wholly-owned subsidiary** [SM 146]
- prescribed classes (Feb 2021): two or more **start-ups**; start-ups with small companies [SM 146]

**Jun'23 case:** a **70% subsidiary** is **not wholly owned**, and a listed company is not small. So the **fast track is not available**; the full s.230–232 NCLT route applies.

### STEPS

1. notice inviting **objections from the ROC, the Official Liquidator** and affected persons within **30 days**
2. objections considered; scheme approved by members holding at least **90% of the total number of shares**
3. each company files a **declaration of solvency** with the ROC
4. approved by **nine-tenths in value of creditors** (meeting on **21 days'** notice, or in writing)
5. transferee files the scheme with the **CG, ROC and OL**
6. no objection → the **CG registers and confirms**. If the ROC or OL objects (within **30 days**), the CG may within **60 days** ask the NCLT to consider it under s.232; silence = no objection

[SM 147–148]

**Effect of registration:** the transferor is **dissolved without winding up**; property, liabilities and charges pass; pending proceedings continue against the transferee; unpaid dues to dissenters become the transferee's liability; shares the transferee holds in itself (or through trusts) are **cancelled**. [SM 148]

## 4 Cross-border merger, dissenters, minority buy-out, and amalgamation by the CG

### s.234 · s.235 · s.230(7)(e) + RULE 27 · s.238

- **s.234 cross-border:** a foreign company (with or without a place of business in India) may merge into an Indian company, or vice versa, with **RBI's prior approval**. Consideration in **cash and/or depository receipts**; only with companies in **notified countries** (Rule 25A). [SM 148]
- **s.235:** where a scheme is approved by holders of **nine-tenths in value** of the shares, the transferee may acquire the **dissenters'** shares: notice to dissenters, their right to apply to the Tribunal, and the consideration kept in a **separate bank account**. [SM 149]
- **Minority exit (s.230(7)(e), Rule 27):** the NCLT may order an exit for dissenters. The minority's shares are valued by a **registered valuer**; their particulars are verified within a **fortnight** of receiving the money; the cut-off date for corporate actions is declared in advance. [SM 149]
- **s.238:** a circular recommending a s.235 offer must carry the prescribed information and the transferee's statement on **cash availability**, and is **registered with the ROC before issue**. Appeal against refusal to the NCLT (the SM misprints "NCCT"). [SM 149]

### s.237: AMALGAMATION ORDERED BY THE CENTRAL GOVERNMENT (Dec'24, Dec'25, MQP)

1. If **essential in the public interest**, the CG may by an **order in the Official Gazette** amalgamate two or more companies into one, with the constitution, property, powers, rights, liabilities and duties the order specifies.
2. The order may continue **pending legal proceedings** by or against the transferee.
3. Every **member, creditor and debenture holder** keeps, as nearly as possible, the **same interest or rights** in the transferee as before.
4. Where the interest or rights are **less** than before, they get **compensation**, assessed by a **prescribed authority**, published in the Gazette, and paid by the transferee.
5. **Remedy:** anyone aggrieved by the assessment may **appeal to the Tribunal within 30 days** of its publication; the Tribunal assesses the compensation.

[SM 149]

## 5 Model answers

**MODEL ANSWER 1 · HOLDING COMPANY + LISTED 70% SUBSIDIARY MERGER (JUN'23 Q4(a)(I), ICMAI PTP MCQ SET) · OUR TOP 1.8 PICK**

**Facts:** ABC Ltd (unlisted public, ₹50 cr capital) holds 70% of BCG Ltd (listed, ₹20 cr). They decide to merge. (i) Is the decision in order? (ii) Must each company's shareholders approve? (iii) What if some shareholders do not consent? (iv) Is an NCLT order required?

1. **In order?** Yes. A merger is a scheme of **reconstruction or amalgamation** under **s.230 read with s.232**, a business decision of the Boards. The draft scheme is adopted by the directors and filed with the ROC. As BCG is **listed**, SEBI and stock-exchange requirements also apply. [SM 145]
2. **Shareholders' approval?** Yes. The NCLT orders meetings of the **members (and creditors) of each company**, and the scheme must be approved by a **majority of persons representing three-fourths in value** in each meeting. [SM 144–145]
3. **Non-consenting shareholders:** once approved and **sanctioned by the NCLT**, the scheme is **binding on all** members, dissenters included. The order may provide for **dissenters** or an **exit offer**. Here the listed transferor merges into an **unlisted** transferee, so ABC **stays unlisted until it lists**, and BCG shareholders who opt out are **paid the value of their shares** per a predetermined price formula or valuation. Only holders of at least **10%** of shares (or **5%** of debt) may object. [SM 143–146]
4. **NCLT order?** Yes. The **fast-track route (s.233)** covers only a holding company with its **wholly-owned** subsidiary, or small companies or start-ups. BCG is a **70%**, listed subsidiary, so the NCLT route under s.230–232 is compulsory. The certified order is filed with the ROC within **30 days**. [SM 146]

**MODEL ANSWER 2 · MINORITY SQUEEZE-OUT IN A RECONSTRUCTION (DEC'23 Q5(b)) · 7 MARKS**

**Facts:** a listed MNC's reconstruction scheme makes the minority sell their shares back to the promoters at a **price fixed by the promoters**, with no choice. Six non-promoter shareholders voted against; the scheme passed with over 90%. The minority say they can reject it. Will they succeed?

1. **Binding effect:** a compromise or arrangement approved by a **majority representing three-fourths in value** and **sanctioned by the NCLT** binds all members, dissenters included (s.230). A 90% vote meets this. [SM 144]
2. **Right to object:** only holders of at least **10%** of shares (or **5%** of debt) may object to the scheme. Six small shareholders below 10% **cannot block it**. [SM 143]
3. **But the price:** the NCLT may order an **exit for dissenting shareholders** (s.230(7)(e)), and the **minority's shares are valued by a registered valuer** (Rule 27), not at a price the promoters fix. The scheme must be **fair**, and the NCLT will not sanction an unfair or unilateral price. [SM 144–149]
4. **Conclusion:** the minority **cannot reject the scheme itself** on numbers. But they can **challenge the valuation before the NCLT** and insist on a price fixed by a registered valuer. If the price is fair and the procedure followed, the squeeze-out stands.
   (⚠ ICMAI's suggested answer is not with us. Courts have upheld such schemes where the majority was overwhelming and the price independently fair; the SM cites no case.)

### SM exercise MCQs on 1.8 (SM 169–171)

| | | | |
|---|---|---|---|
| 70 in a merger the transferor company is | **dissolved** | 72 transferred on amalgamation | **rights and liabilities (both)** |
| 71 the auditor confirms the scheme | **conforms to the accounting standards** | 73 listed transferor into an unlisted transferee | **stays unlisted unless it lists** |
| 84 A Ltd merges with B Ltd: A Ltd is | **dissolved** | bank 252 "mutatis mutandis" | **subject to necessary modifications** |

## R Revision: every number in 1.8

| Rule | Number |
|---|---|
| CDR consent: secured creditors in value | 75% |
| regulators' representations within | 30 days |
| objection only by: shareholding / debt | ≥ 10% / ≥ 5% |
| shareholding changes disclosed for last | 6 months |
| approval: majority + value | ¾ in value |
| dispense with creditors' meeting if they consent | 90% in value |
| order to ROC / compliance statement | 30 / 210 days |
| takeover within scheme: holding at least | ¾ of shares |

| Rule | Number |
|---|---|
| supplementary accounts if last accounts older than | 6 months |
| s.233: objections / members / creditors | 30 days / 90% shares / 9/10 value |
| s.233 creditors' meeting notice | 21 days |
| s.233: ROC/OL objection / CG to NCLT | 30 / 60 days |
| s.235 approval | 9/10 in value |
| minority particulars verified within | a fortnight |
| s.237 appeal to Tribunal within | 30 days |

# 1.9 · Prevention of Oppression and Mismanagement P13 · Module 1 · s.241–246 + Foss v. Harbottle

SM pp. 150–157 (8 pages). 29 marks in 7 papers, asked in 6. Long questions in 4, **but only MCQs in the last two**. The eligibility rule (s.244) is asked again and again.

| Paper | What was asked | Marks |
|---|---|---|
| Jun'23 | Q3(a) petitioners hold **12%**; members holding 5% withdraw mid-way and ask for dismissal: maintainable? | 4 |
| Jun'24 | Q2(a) **class action** (s.245) and the remedies | 7 |
| Dec'24 | Q5(b) 600 members; **90 members** holding 10,000 of 5 lakh shares file: maintainable? 40 withdraw? fewer than required: **waiver**? | 7 |
| Jun'25 | Q7(a) **exceptions to Foss v. Harbottle** | 7 |
| Dec'25 | MCQ: who may apply under s.241 (= MCQ bank 97) | 2 |
| Jun'26 | MCQ case: can a **12%** minority apply? | 2 |

**DEC'26 PREDICTION**

Tier **B**, **2–9 marks**: an MCQ or a 7-marker. The likely 7-marker is **"who can apply; waiver; withdrawal of consent"** (asked in Jun'23 and Dec'24, and in ICMAI's PTP). The **Tribunal's powers (s.242)** have never been asked.

**MAP**

1. Majority rule and Foss v. Harbottle; exceptions ★★
2. Oppression: meaning, who applies (s.241, 244) ★★★
3. Powers of the Tribunal (s.242, 243) ★
4. Class action (s.245) ★★
5. Model answers · MCQs · numbers

## 1 Majority rule, Foss v. Harbottle and its exceptions · Jun'25 Q7(a)

### THE RULE

- **Majority rules:** a resolution of the majority at a properly held meeting, on a matter within the company's powers, **binds the minority** (*North-West Transportation v. Beatty*). Where a **special resolution** is needed, a three-fourths majority is required (*Edwards v. Halliwell*). [SM 151]
- **Foss v. Harbottle (1843):** courts do **not interfere in internal management**. For a wrong done to the company, the **company is the proper plaintiff**, not an individual member (*Gray v. Lewis*). The reason: a member agrees to accept the majority's will. [SM 151]

### EXCEPTIONS (common law): A MEMBER MAY SUE

a. **ultra vires or illegal acts**: an injunction to restrain them
b. **fraud on the minority**
c. **wrongdoers in control**, who would never let the company sue (*Birch v. Sullivan*; *Edwards v. Halliwell*)
d. a **special-majority act passed by a simple majority**, or a special resolution on insufficient notice (*Baillie v. Oriental Telephone*)
e. **personal rights**: to vote, have the vote recorded, stand for election (*Nagappa Chettiar v. Madras Race Club*; *Salmon v. Quin & Axtens*)
f. **breach of duty** by directors and the majority, even without fraud (*Daniels v. Daniels*: land sold to a director's wife for £4,250 and resold for £1,20,000)

[SM 151–152]

**Statutory exceptions (the Companies Act):** relief against **oppression and mismanagement** (s.241–244), **class action** (s.245), and the Central Government's power to apply. These are parts 2–4 below. [SM 151]

## 2 Oppression and mismanagement: meaning, grounds, who may apply (s.241, s.244)

**WHAT IT IS** "**Oppression**" and "**mismanagement**" are **not defined** in the Act (MCQ bank 250). Oppression is conduct showing **"a visible departure from the standards of fair dealing"** on which every shareholder is entitled to rely (*Elder v. Elder & Watson*, approved in *Shanti Prasad Jain v. Kalinga Tubes*). The burden on the shareholder must be **unjust, harsh or tyrannical** (*Scottish Co-op v. Meyer*). [SM 152–153]

### GROUNDS (s.241(1)): A MEMBER MAY APPLY WHERE

a. the company's affairs are conducted **prejudicially to the public interest**, or **oppressively or prejudicially** to him or other members, or prejudicially to the company; or
b. a **material change in management or control** (Board, manager, share ownership, membership) makes such conduct likely

... provided he has the **right to apply under s.244**. Applications go to the **Tribunal (NCLT)**. [SM 153]

**Central Government:** may itself apply if affairs are prejudicial to the **public interest** (before the **Principal Bench**). Since the 2019 amendment it may also refer cases of **fraud, misfeasance, persistent negligence or breach of trust**, unsound business practice, injury to the trade, or an intent to defraud creditors or members (s.241(3)). [SM 153–154]

### WHO MAY APPLY (s.244): LEARN THESE NUMBERS

| | |
|---|---|
| **Company with share capital** | at least **100 members**, OR at least **one-tenth of total members**, **whichever is less**; OR members holding at least **one-tenth of the issued share capital**. All calls and dues on their shares must be paid |
| **Without share capital** | at least **one-fifth** of total members |
| **Waiver** | the Tribunal may, on application, **waive any or all** of these requirements |
| **On behalf of all** | one or more eligible members may apply with the **written consent of the rest** |

[SM 153]

### ⚠ WITHDRAWAL OF CONSENT MID-WAY (Jun'23 Q3(a), Dec'24 Q5(b)(ii)): NOT IN THE SM

The Supreme Court held in *Rajahmundry Electric Supply Corp. v. A. Nageswara Rao* (1956) that the **validity of the petition is judged on the facts at the time it is filed**. If the consenting members met the s.244 requirement on that date, **later withdrawal of consent by some of them does not make the petition non-maintainable**. The case is from the old Act (s.399, 1956), but the principle is applied under s.244.

## 3 Powers of the Tribunal (s.242) and termination of agreements (s.243): never asked yet

If the Tribunal finds the affairs oppressive or prejudicial, and that **winding up would unfairly prejudice** the members although the facts would justify a "just and equitable" winding up, it may make **any order it thinks fit** to end the matters complained of, including: [SM 154]

1. **regulating** the company's future conduct
2. **purchase of shares** of members by other members or by the company, with the consequent **reduction of capital**
3. **restrictions** on transfer or allotment of shares
4. **terminating, setting aside or modifying agreements** with the MD, directors or manager, or (with notice and their consent) with others
5. **setting aside transfers, payments or acts** within **3 months** before the application that would be a **fraudulent preference** in insolvency
6. **removing the MD, manager or directors**, and deciding how a new MD is appointed
7. **recovering undue gains** of managerial persons
8. **appointing directors** who report to the Tribunal
9. **costs**, and anything else just and equitable; **interim orders**

The certified order is filed with the ROC within **30 days**. If the order alters the MOA or AOA, the company **cannot make inconsistent alterations**. [SM 155] (SM MCQ 78: powers in s.242.)

**s.243:** a terminated agreement gives **no claim** to damages or compensation for loss of office. The person may **not be appointed or act** as MD, director or manager of the company for **5 years** without the Tribunal's leave (with notice to the CG). A person held **unfit** under s.242(4A) cannot hold office for **5 years** without CG and Tribunal approval. Acting in breach: fine up to **₹5 lakh**. [SM 155]

## 4 Class action (s.245) · Jun'24 Q2(a)

**WHAT IT IS** Members or depositors (or a class of them) who think the company's affairs are conducted **prejudicially to the company, its members or depositors** may file **one application before the Tribunal on behalf of all of them**. Any person, group or association representing those affected may file it.

[SM 155–157]

### REMEDIES THAT MAY BE SOUGHT

1. restrain an act **ultra vires** the MOA or AOA, or a breach of them
2. **declare void** a resolution altering the MOA or AOA passed by **suppressing material facts** or misstatement, and restrain acting on it
3. restrain acts **contrary to the Act or any law**, or contrary to members' resolutions
4. **damages or compensation** from: the company or directors (fraudulent, unlawful or wrongful acts); the **auditor or audit firm** (misleading audit report); any **expert, advisor or consultant** (misleading statements)
5. any other remedy the Tribunal thinks fit

[SM 155–156]

### WHO, AND HOW THE TRIBUNAL HANDLES IT

- **Members:** at least **100**, or the prescribed % of members (whichever is less), or holders of the prescribed % of issued capital, with calls paid. Without share capital: **one-fifth**. **Depositors:** at least **100**, or the prescribed %, or those owed the prescribed % of deposits. [SM 156]
- On admission: **public notice** to the class · similar applications **consolidated**, with a **lead applicant** chosen by the class or appointed by the Tribunal · **no two class actions on the same cause** · **costs** borne by the company or the wrongdoer. [SM 156]
- The order **binds** the company, members, depositors, auditors, experts and advisors. [SM 157]
- **Non-compliance:** company **₹5 lakh to ₹25 lakh**; officers up to **3 years** in jail and a fine of **₹25,000 to ₹1 lakh**. [SM 157]
- Does **not apply to banking companies**. Sections **337–341** (fraud and damages) apply to s.241 and s.245 proceedings (s.246). [SM 157]

## 5 Model answers

**MODEL ANSWER 1 · WHO CAN APPLY, WITHDRAWAL, WAIVER (DEC'24 Q5(b)) · 7 MARKS**

**Facts:** a public company has **600 members** and issued capital of ₹5 crore (**5 lakh shares** of ₹100). **90 members** holding **10,000 shares** petition the Tribunal against oppression and mismanagement. (i) Is it maintainable? (ii) What if 40 members later withdraw consent? (iii) If the members are fewer than required, can they still apply?

1. **Law (s.244):** in a company with share capital, at least **100 members or one-tenth of the members, whichever is less**, OR members holding at least **one-tenth of the issued capital**, with calls paid, may apply under s.241. The Tribunal may **waive** the requirements. [SM 153]
2. **(i)** One-tenth of 600 = **60**, which is less than 100, so **60 members** suffice. The 90 petitioners exceed 60, so the petition is **maintainable**, even though their 10,000 shares are only 2% of capital. Either test is enough.
3. **(ii)** If 40 withdraw, 50 remain, below 60. But maintainability is judged **on the date of filing**; on that date 90 members had consented. Later withdrawal **does not make the petition non-maintainable** (*Rajahmundry Electric Supply v. Nageswara Rao*, SC). The Tribunal continues.
4. **(iii)** Yes. Under the **proviso to s.244(1)**, the Tribunal may, on an application, **waive all or any of the requirements** so that the members can apply under s.241. [SM 153]

**MODEL ANSWER 2 · THE 12% CASES (JUN'23 Q3(a); JUN'26 MCQ (iv))**

**Jun'23:** petitioners hold **12%** of issued capital; some, holding **5%**, withdraw and join the majority asking for dismissal. At filing, 12% was at least **one-tenth of the issued capital**, so the petition was validly filed. On the *Rajahmundry* principle, the **later withdrawal does not affect maintainability**, and the contention of the withdrawing group and the majority **fails**. [SM 153]

**Jun'26 MCQ:** can a 12% minority apply? **(B) Yes, directly under s.241**. 12% exceeds the one-tenth test, so no waiver or permission is needed. Option (C), "with the Tribunal's permission", applies only when the s.244 numbers are **not** met. [SM 153]

### SM exercise / MCQ bank on 1.9

| | | | |
|---|---|---|---|
| 74 powers of the majority are subject to | **the Act, common law, MOA: all** | 78 the Tribunal's powers are in section | **242** |
| 75 an act beyond the directors' authority | **ultra vires** | bank 97: who may apply under s.241 ★ | **any of the above** |
| 76 an oppression application may be made on | **fraud on minority, ultra vires, breach of duty: any or all** | bank 250: oppression and mismanagement are defined in | **none (not defined)** |
| 77 relief against oppression is sought from | **the Tribunal (NCLT)** ⚠ | bank 251: may also apply if affairs prejudice the public interest | **Central Government** |

⚠ The MCQ bank's key for SM MCQ 77 says "ROC". That is wrong: s.241 and s.244 applications go to the **Tribunal (NCLT)**, as the SM text says.

## R Revision: every number in 1.9

| Rule | Number | Rule | Number |
|---|---|---|---|
| s.244: members (share capital) | 100 or 1/10, less | s.243 bar on re-appointment | 5 years |
| s.244: share capital held | ≥ 1/10 of issued | s.243 fine | ≤ ₹5 lakh |
| s.244: no share capital | 1/5 of members | class action: members / depositors | 100 (or prescribed %) |
| fraudulent preference look-back | 3 months | s.245 company fine | ₹5–25 lakh |
| s.242 order to ROC within | 30 days | s.245 officer: jail / fine | 3 yrs / ₹25,000–₹1 lakh |
| special resolution majority | ¾ | s.246 applies sections | 337–341 |

# 1.3 · Dividends P13 · Module 1 · Chapter VIII, s.123–127 + IEPF

SM pp. 44–50 (7 pages). 14 marks in 7 papers. Long in Jun'23 (a case) and **Jun'26 (declaration and payment, 7 marks)**; the rest MCQs. ICMAI's PTP repeated the Jun'26 question.

| Paper | What was asked | Marks |
|---|---|---|
| Jun'23 | MCQ: dividend distribution policy is decided by the **Board** · Q3(c) **failure to pay**: a bank mandate failed and the shareholder was not told; a court order stopped payment | 2 + 3 |
| Dec'23 | MCQ: dividend deposited in a separate account within **5 days** (s.123(4)) | 2 |
| Jun'26 | Q2(a) **statutory provisions on declaration and payment of dividend** | 7 |

**DEC'26 PREDICTION**

Tier **B**, **2–7 marks**. Dividend was the long question in Jun'26, so expect an **MCQ**. If a long question comes, the fresh part is the **unpaid dividend account and the IEPF** (s.124/125, never asked).

## 1 Meaning, sources of dividend, and dividend out of reserves (s.2(35), s.123)

**WHAT IT IS** **Dividend** (s.2(35)) **includes interim dividend**: the part of profit **not retained** but distributed to shareholders in proportion to the amount paid up on their shares. A **final dividend** is declared at the **AGM on the Board's recommendation**; an **interim dividend** is declared by the **Board** between AGMs. **Section 8** companies cannot pay dividend. [SM 44]

### DECLARED ONLY OUT OF (s.123(1))

a. the **current year's profit**, after **depreciation**
b. **undistributed profits of previous years**, after depreciation
c. both

- Profits **exclude unrealised or notional gains, revaluation** and fair-value changes. [SM 45]
- **Not out of reserves other than free reserves.** Carried-forward losses and depreciation are set off first. [SM 45]
- A company that has **failed to repay public deposits** or interest (s.73, 74) **cannot declare dividend**. [SM 45]
- It may first transfer any percentage of profits to reserves. [SM 45]

### OUT OF FREE RESERVES, IN A LOSS OR LOW-PROFIT YEAR (Rule 3)

1. rate not above the **average rate of the 3 preceding years** (not applicable if no dividend was declared in each of those 3 years) (MCQ bank 254)
2. amount drawn not above **one-tenth** of (paid-up capital + free reserves) per the latest audited FS
3. the amount drawn is **first used to set off the year's losses**, before any equity dividend
4. reserves left must be at least **15%** of paid-up capital

[SM 45]

## 2 Interim dividend, depositing, payment, and failure to pay (s.123(3)–(5), s.127)

### INTERIM DIVIDEND s.123(3)

- Declared by the **Board** (SM MCQ 88; PTP and postal MCQs) during the year, or between the year-end and the AGM, out of the P&L surplus or the year's profits (up to the quarter before declaration). [SM 46]
- If there is a **loss** up to the end of the preceding quarter: rate not above the **average of the 3 preceding years**. [SM 46]
- **Ratified at the AGM** with the final dividend. [SM 46]

**Deposit (s.123(4)):** the dividend, interim included, goes into a **separate account in a scheduled bank within 5 days** of declaration (Dec'23 MCQ; SM MCQ 26). Not for 100% Government companies. [SM 45–46]

### PAYMENT s.123(5)

- A dividend **once declared at the AGM cannot be revoked** (SM MCQ 24). [SM 46]
- Payable **in cash**: by cheque, warrant or electronic mode, only to the **registered shareholder**, his order or his banker. [SM 46]
- **Bonus shares** (capitalisation of profits) are not dividend. [SM 46]

### s.127: FAILURE TO DISTRIBUTE

- Every director **knowingly party** to the default: up to **2 years** in jail, and a fine of at least **₹1,000 a day** while it continues. [SM 46]
- The company pays **simple interest at 18% a year** for the period of default. [SM 46]

**No offence where:** (1) a **law** prevented payment; (2) the **shareholder's directions** could not be complied with **and this was communicated to him**; (3) there is a **dispute** about the right to receive it; (4) it was **lawfully adjusted** against a sum the shareholder owed; (5) the failure was **not due to any default** of the company. [SM 46–47]

### ⚠ TIME LIMITS THE SM DOES NOT STATE

**s.127:** a declared dividend must be **paid within 30 days** of declaration; the offence is not paying within that time.
**s.124(1):** any amount still unpaid is moved to an **Unpaid Dividend Account** within 7 days after those 30 days end.
**s.124(6): shares** on which dividend has gone unpaid for **7 consecutive years** are also transferred to the IEPF. Use these in a full answer.

## 3 Unpaid dividend and the IEPF (s.124, s.125): never asked yet

**TRANSFER TO THE IEPF**

1. Money in the **unpaid dividend account** unclaimed for **7 years** from its transfer goes, with interest, to the **Investor Education and Protection Fund** (SM MCQ 25; MCQ bank 256). [SM 48]
2. Remitted within **90 days** of becoming due; a statement in **Form DIV-5** goes to the IEPF Authority. [SM 48]
3. The company keeps records (names, addresses, amounts, folio and certificate numbers) of those whose money was transferred, for **8 years**. [SM 48]
4. A claimant applies to the **IEPF Authority** for a refund. [SM 48]

**WHAT GOES INTO THE FUND · WHAT IT IS USED FOR**

**Credited:** CG grants; donations from Governments and companies; unpaid dividend accounts; old s.205A/205C balances; income on investments; s.38(4) penalties; application money due for refund; **matured deposits** and **debentures** with interest; sale proceeds of **fractional shares** and **unpaid preference redemption** amounts after **7 years**. [SM 47–48]

**Used for:** refunds of unclaimed amounts · investor education, awareness and protection · distributing **disgorged amounts** to victims · **legal expenses of class actions** (s.37, s.245) sanctioned by the Tribunal. The **Authority**: a chairperson, up to **7** members and a CEO. [SM 48–49]

**Dividend distribution policy (LODR Reg 43A):** the **top 1,000 listed entities** by market capitalisation (as on 31 March) must have one, disclosed in the annual report and website. It covers: when shareholders may or may not expect dividend; financial parameters; internal and external factors; use of retained earnings; parameters for each class of shares. The **Board** decides it (Jun'23 MCQ). Types: interim, final, special. [SM 49–50]

## 4 Model answers

**MODEL ANSWER 1 · FAILURE TO DISTRIBUTE (JUN'23 Q3(c)) · 3 MARKS**

**Facts:** VS Computers paid all its dividend on time except (i) Mrs AB's: her bank returned it because of a surname mismatch, and the company **did not inform her**; (ii) ₹50,000 due to the successor of the late Mr PR, which a **court order restrained** because of a family succession dispute.

**Law:** under s.127, failure to pay a declared dividend makes every director knowingly party to it liable to up to **2 years** in jail and a fine of at least **₹1,000 a day**, and the company pays **18%** interest. No offence where the shareholder's directions **could not be complied with and this was communicated to him**, or where a **law** or a **dispute over entitlement** prevents payment. [SM 46–47]

**(i) Mrs AB:** her mandate could not be complied with, but the company **did not communicate this** to her, so the exception is **not available**. The company is **in default**; the directors responsible are liable and interest at 18% is payable. **(ii) Mr PR's successor:** payment was stopped by a **court order** in a **dispute regarding the right to receive** the dividend. Both exceptions apply, so **no offence**.

**ANSWER FRAME · DECLARATION AND PAYMENT OF DIVIDEND (JUN'26 Q2(a), ICMAI PTP Q2(a)) · 7 MARKS**

1. **Meaning** (s.2(35)); final dividend at the AGM on the Board's recommendation; interim dividend by the Board.
2. **Sources** (s.123(1)): current or past profits after depreciation; no unrealised gains; free reserves only; carried-forward losses set off; **no dividend while public deposits are in default**.
3. **Out of free reserves**: the four Rule 3 conditions (3-year average, one-tenth, losses first, 15% left).
4. **Interim dividend**: the loss-quarter limit (3-year average); ratified at the AGM.
5. **Deposit** in a scheduled bank within **5 days**; **payment** in cash or electronically to the registered holder; cannot be revoked.
6. **Failure (s.127)**: penalties, 18% interest, exceptions; unpaid amounts → Unpaid Dividend Account → IEPF after 7 years.

[SM 44–48]

### SM exercise / MCQ bank on 1.3

| | | | |
|---|---|---|---|
| 24 once declared at the AGM, a dividend | **cannot be revoked** | 85 dividend distribution policy decided by ★ | **Board of Directors** |
| 25 IEPF | **Investor Education and Protection Fund** | 88 interim dividend decided by | **Board of Directors** |
| 26 / bank 255: separate account within ★ | **5 days** | bank 254: rate cap = average of last | **3 years** |
| bank 256: unclaimed 7 years goes to | **IEPF** | bank 260: not a type of dividend | **"mid-term dividend"** |

### Numbers

deposit within **5 days** · rate cap: average of **3** years · draw at most **1/10** of (PUC + FR) · reserves left **≥ 15%** · s.127: **2 years**, **₹1,000/day**, **18%** · IEPF after **7 years**, remit in **90 days**, DIV-5, records kept **8 years** · Authority: up to **7** members · Reg 43A: top **1,000** listed entities.

# 1.7 · Inspection, Inquiry and Investigation P13 · Module 1 · Chapter XIV, s.206–229

SM pp. 133–140 (8 pages). The **lowest-weight** Companies Act topic: 6 marks in 7 papers (Jun'23 4-mark case; Dec'23 MCQ on "seizure"). Tier **C**: learn the definitions and numbers for an MCQ.

### THREE WORDS (SM)

- **Inspection**: a careful look or official visit to check that everything is **correct and legal**; **routine, not negative**. [SM 133]
- **Inquiry**: an official process to **discover facts** about something bad; negative unless the report is clean. [SM 133]
- **Investigation**: a **deeper probe** to gather evidence for prosecution of a suspected violation; always negative. Inspection may lead to investigation. [SM 133]
- **Seizure**: the **forcible taking of property** by a law-enforcement official from a person suspected of violating the law (Dec'23 MCQ). **Search**: an examination of records to confirm ownership and claims. [SM 135]

### REGISTRAR'S POWERS (s.206, s.207)

- **Call for information:** on scrutiny of documents or information received, the ROC may by **written notice** require information, explanations or documents within a reasonable time; past officers too. If not given, inadequate, or affairs unsatisfactory → a **further notice** to produce books for inspection (reasons recorded). [SM 133–134]
- **Inquiry (s.206(4)):** if satisfied (on information or **anyone's representation**) that the business is carried on for a **fraudulent or unlawful purpose**, or in breach of the Act, or **investor grievances** are not addressed: the ROC informs the company of the allegations in a **written order**, gives it a **reasonable opportunity of being heard**, and inquires. The **CG may direct** the ROC or an inspector to inquire. Fraud → officers liable under **s.447**. [SM 134]
- The CG may also order **inspection** by an inspector or a statutory authority (s.206(5)). [SM 134]
- Directors, officers and employees must produce documents and assist. The ROC or inspector has **civil court powers (CPC)**: discovery, summons and examination on oath, inspection anywhere (SM MCQ 69). [SM 135]
- **Disobedience:** up to **1 year** in jail and a fine of **₹25,000 to ₹1 lakh**. On conviction, the director or officer **vacates office** and is disqualified. [SM 135]

## 1 Search and seizure, inspection report, investigation, SFIO

### SEARCH AND SEIZURE (s.209) · REPORT (s.208)

- If the ROC or inspector believes books of the company, its KMP, directors, auditor or CS are likely to be **destroyed, mutilated, altered, falsified or secreted**: with an order of the **Special Court**, he may enter, search and seize. [SM 135–136]
- Return them as soon as possible; they may be called for again for a further **180 days**. The CrPC applies to searches. [SM 136]
- **s.208:** the inspecting person reports to the **CG**, possibly recommending further investigation. [SM 136]

⚠ The SM prints the return deadline as the "one hundred and eighteenth day". The Act says the **180th day**.

### INVESTIGATION (s.210, 212, 213)

- **s.210:** the **CG** may order an investigation on an ROC or inspector's report, on the company's **special resolution**, or in the **public interest**. It **must** order one if a court or the **Tribunal** so orders. [SM 136]
- **s.212 SFIO** (Serious Fraud Investigation Office, SM MCQ 62): the CG may assign the investigation to the SFIO on the same grounds, or **on request of a CG or State department**. Then **no other agency** proceeds under this Act and records are transferred. The SFIO Director appoints an investigating officer with inspector's powers; interim and final reports go to the CG, which may direct **prosecution**. [SM 136–137]
- **s.213 (on application to the NCLT):** by at least **100 members** or holders of **one-tenth of voting power** (share capital), or **one-fifth** of members (no share capital), with evidence. Or by any person, if there is intent to defraud, oppression, fraud or misfeasance in formation or management, or members are denied information. The Tribunal may order an investigation by inspectors appointed by the CG; if allegations are proved, **s.447** applies. [SM 137]

### OWNERSHIP, INSPECTORS, EMPLOYEES

- **s.216:** the CG may investigate **ownership**: who is financially interested, who controls or influences policy, and who are the **beneficial owners**. [SM 137–138]
- **s.217:** officers, employees and agents (past ones too) preserve and produce books and assist. The inspector keeps books at most **180 days** (+ **180** more if needed again). **Civil court powers**; help from police and authorities; reciprocal arrangements with foreign States. [SM 138]
- **s.218:** during an investigation, the company needs **Tribunal approval** to discharge, suspend, punish or worsen the terms of any employee (SM MCQ 68: NCLT). If there is no reply within **30 days**, it may proceed; appeal to the NCLAT within **30 days**. [SM 138–139]

### RELATED BODIES, SEIZURE, RESTRICTIONS, AFTERMATH

- **s.219:** an inspector may also investigate the **holding or subsidiary** companies, bodies managed by the same MD, bodies whose Board follows the company, and past MDs or employees, **with CG approval**. [SM 139]
- **s.220:** the inspector may **seize** books likely to be destroyed, after allowing copies, and keep them until the investigation ends. [SM 139]
- **Restrictions on securities:** the Tribunal may impose them for up to **3 years**, and freeze assets. [SM 139–140]
- **s.224:** the CG may **prosecute**, or bring proceedings in the company's name for **damages or recovery of property** (with indemnity for costs). **s.225:** expenses are paid first by the CG and recovered from convicted persons, the company, or the applicants. [SM 140]

**ANSWER FRAME · ROC INQUIRY ON SHAREHOLDERS' COMPLAINT (JUN'23 Q2(a))**

**(i) Power:** yes. Under s.206(4) the ROC may inquire where, on information or a **representation by any person**, he is satisfied that the business is carried on for a **fraudulent or unlawful purpose**. **(ii) Procedure:** inform the company of the allegations by **written order** → call for information or explanations → give a **reasonable opportunity of being heard** → inquire, with **civil court powers** → report to the CG (s.208). **(iii) Complaint withdrawn:** the inquiry is the ROC's **statutory function** in the public interest once he is satisfied, so it is not tied to the complainants and **may continue** (reasoning; the SM is silent). **(iv)** The **CG may direct** the ROC or an inspector to carry out the inquiry. [SM 134–136]

| | | | |
|---|---|---|---|
| 62 SFIO | **Serious Fraud Investigation Office** | 68 punishing an employee during investigation needs | **NCLT approval** |
| 67 investigation is in chapter | **XIV** | 69 investigator's powers per | **Civil Procedure Code** |

**Numbers:** s.207 jail **1 yr**, fine **₹25,000–₹1 lakh** · seized books returned by the **180th** day (SM misprint) + **180** · s.213: **100** members / **1/10** voting power / **1/5** members · inspector holds books **180 + 180 days** · s.218: **30 days** / appeal **30 days** · securities restricted up to **3 years**.

# Module 2 · Insolvency and Bankruptcy Code, 2016 P13 · Section A · topics 2.1–2.4

SM pp. 185–216 (32 pages). **55 marks in 7 papers**, almost all on **2.2 CIRP**. A 7-mark IBC long question in **5 papers running** (Jun'24 → Jun'26), plus 1–2 MCQs. Liquidation (2.3) and personal insolvency (2.4) have never had a long question.

Section numbers the SM does not print are taken from the Act.

| Paper | What was asked | Marks |
|---|---|---|
| Jun'23 | Q3(d) **applicability** of the IBC | 4 |
| Dec'23 | nothing | 0 |
| Jun'24 | MCQ: the IBBI has **civil court** powers (= SM MCQ 14) · MCQ: CIRP in **180 days** (= SM MCQ 5) · Q2(b) **persons not entitled to initiate CIRP** (s.11) | 2 + 2 + 7 |
| Dec'24 | MCQ: no IP proposed → AA asks the Board in **7 days**, Board nominates in **10** (SM 2.4.2 text) · MCQ: extension needs **66%** of CoC · Q4(a) **s.28 prior approval of the CoC** + voting % | 2 + 2 + 7 |
| Jun'25 | MCQ: IBC not applicable to **financial service providers** (= SM MCQ 12) · MCQ: **s.29A** (= SM MCQ 19) · Q2(b) **management of affairs by the IRP** | 2 + 2 + 7 |
| Dec'25 | MCQ: CIRP with extension = **270 days** · Q5(b) **approval of the resolution plan by the NCLT** | 2 + 7 |
| Jun'26 | MCQ: **270 days** again (verbatim Dec'25) · Q5(b) case: **CIRP by a financial creditor**; role of the NCLT, RP duties, plan approval | 2 + 7 |

**HOW IT IS EXAMINED · DEC'26 PREDICTION**

- Long answers are **SM paragraphs** (s.11, s.28, IRP management). MCQs are SM exercise MCQs or SM sentences.
- **Q5(b), 7 marks, about 75% likely.** Our picks: (1) **fast-track CIRP** (ICMAI MQP Q5(a); not in the SM, see the ⚠ box); (2) **s.28** again (MQP Q5(b)); (3) the **2026 amendment** (both supplementaries); (4) the PTP case: an **NBFC lender**; (5) **moratorium** (never asked).
- MCQ: timelines (**180 / 270 / 330**), CoC percentages, 7 and 14 days.

**MAP**

1. Purpose, applicability, five pillars ★★
2. Definitions; financial vs operational creditor ★★
3. CIRP: s.11, initiation s.7/9/10, timeline ★★★
4. Moratorium, IRP, CoC, RP, s.28 ★★★
5. Resolution plan: s.29A, s.30, s.31 ★★★
6. Liquidation and s.53 waterfall ★
7. Personal insolvency ★
8. Model answers · SM exercise · numbers

## 2.1 Purpose, applicability, regulators · Jun'23 Q3(d), Jun'25 MCQ, postal Q3(b)

**WHY THE CODE · PURPOSE (SM ESSAY 1)**

- It replaced **multiple overlapping laws and forums**: Ch. XIX and XX of the Companies Act 2013; Part VIA, Part VII and s.391 of the 1956 Act; RDDBFI 1993; SARFAESI 2002; **SICA 1985**; the Presidency Towns (1909) and Provincial (1920) Insolvency Acts; Ch. XIII of the LLP Act 2008 (SM MCQ 13). [SM 187]
- Drafted by the **Bankruptcy Law Reforms Committee**; Bill in Nov 2015; passed in 2016 (SM MCQ 1). [SM 187]
- SM WORDS **Purpose:** (1) to consolidate and amend the laws relating to **reorganization and insolvency resolution** of corporate persons, partnership firms and individuals **in a time bound manner** for **maximization of value of assets**, to **promote entrepreneurship and availability of credit**; (2) **balance the interests of all the stakeholders**, including alteration in the order of priority of payment of Government dues; (3) establish the **Insolvency and Bankruptcy Board of India**. [SM 187–188]

**APPLICABILITY (s.2) · THE JUN'23 ANSWER**

Whole of India. Applies to insolvency, liquidation, voluntary liquidation or bankruptcy of: (a) **companies** under the Companies Act; (b) companies under a **special Act**; (c) **LLPs**; (d) other body corporates notified by the CG; (e) **personal guarantors** to corporate debtors; (f) **partnership and proprietorship firms**; (g) **individuals**. [SM 188]

**Not** to the finance sector: a "corporate person" **excludes a financial service provider** (s.3(7)), so banks, FIs, insurers, ARCs, mutual funds, CIS and pension funds are outside it (SM MCQ 3; SM MCQ 12 = Jun'25 MCQ). [SM 188]

**Five pillars: IBBI** (the regulator, SM MCQ 16; has **civil court** powers for summons, discovery, inspection, commissions: SM MCQ 14 = Jun'24 MCQ) · **Adjudicating Authority** (NCLT for companies and LLPs; **DRT** for individuals and firms) · **Insolvency Professional Agencies** · **Insolvency Professionals** · **Information Utilities**. [SM 188, SM 210]

### Key definitions (s.3 and s.5)

**Corporate person**: a company, an LLP, or any other body with limited liability, **but not a financial service provider** [s.3(7)].
**Corporate debtor**: a corporate person who **owes a debt** to any person [s.3(8)]. [SM 189]

**Creditor**: anyone to whom a debt is owed: financial, operational, secured, unsecured creditors and decree holders. **Debt**: a liability for a claim due from any person, including financial and operational debt. **Claim**: a right to payment, whether or not fixed, matured, disputed, secured or not. **Default**: non-payment of debt, in whole, in part or an instalment, when due. [SM 189]

**Financial debt** [s.5(8)]: debt disbursed **against consideration for the time value of money**, e.g. money borrowed against interest, bonds and debentures, finance leases, receivables sold with recourse, and **amounts raised from real-estate allottees**, which are deemed borrowings. [SM 189–190]

**Operational debt**: a claim for **goods or services, including employment**, or **dues under any law to the Central or State Government or a local authority**. [SM 190]

**Person** [s.3(23)]: an individual, HUF, company, trust, partnership, LLP, any statutory entity, and a **person resident outside India** (SM MCQ 18). [SM 190]

**Adjudicating Authority** for corporate persons = **NCLT** under s.408 of the Companies Act, 2013 [s.5(1)]. [SM 190]

**Corporate applicant** [s.5(5)]: the corporate debtor; an authorised member or partner; the individual managing its operations; or the person controlling its financial affairs. [SM 191]

**Insolvency commencement date** = the date the AA **admits** the application under s.7, 9 or 10 (the **initiation date** is the date of filing). **Insolvency resolution process period** = **180 days** from the commencement date. [SM 191]

**Related party** [s.5(24)]: directors, partners, KMP and their relatives; a company where a director holds over **2%**; holding, subsidiary and associate companies; a person controlling over **20%** of votes (either way); anyone controlling the board; more than **two directors in common**; anyone on whose advice a director is accustomed to act (SM MCQ 17, essay 2). [SM 191–192]

**Resolution plan**: a plan by a resolution applicant to resolve the corporate debtor **as a going concern**; it may include merger, amalgamation or demerger. **Resolution professional**: the IP who runs the CIRP, including the IRP. **Voting share**: in proportion to the **financial debt** owed. [SM 192]

| | Financial creditor (FC) | Operational creditor (OC) |
|---|---|---|
| owed | financial debt (incl. a debt legally assigned to him) [s.5(7)] [SM 189] | operational debt: goods, services, employment, Government dues [s.5(20)] [SM 190–191] |
| to start CIRP | **files directly** with the NCLT (s.7), alone or jointly, with a record of default | first serves a **demand notice** or invoice; files (s.9) only if **not paid or disputed within 10 days** [SM 195] |
| in the CoC | **member with votes** (unless a related party) [SM 199] | **no vote**; one representative may attend if OCs' dues are at least **10%** of the debt [SM 200] |

## 2.2 Corporate insolvency resolution process (CIRP) · the Q5(b) topic

**Default** min. ₹1 lakh in the SM [SM 193] → **Application** FC s.7 · OC s.9 · CD s.10 → **NCLT admits** within 14 days; 7 days to fix defects [SM 194–195] → **Moratorium + public announcement + IRP** → **CoC** of FCs; 1st meeting within 7 days; RP by 66% [SM 199] → **Plans** → CoC 66% → **NCLT** (s.31) [SM 202]

**⚠ TWO SM FIGURES ARE OUT OF DATE (NOT IN SM)**

(1) The minimum default was raised from ₹1 lakh to **₹1 crore** by notification of 24 March 2020; the SM only says the CG "can increase" it up to ₹1 crore. (2) The SM's outer limit of "360 days including any extension" should be **330 days**: the 2019 amendment set 330 days, **including time taken in legal proceedings**.

### WHO MAY START (s.6) · WHO MAY NOT (s.11) · JUN'24 Q2(b)

On a default, a **financial creditor**, an **operational creditor** or the **corporate debtor itself** may start a CIRP. [SM 193]

SM WORDS A corporate debtor (including a corporate applicant) **shall not be entitled** to apply:

a. when it is **undergoing a CIRP** or a pre-packaged process; also an FC or OC of a debtor undergoing a **pre-packaged** process;

b. when it **completed a CIRP**, or had a pre-pack plan approved, within **twelve months** before the application;

c. a corporate debtor or FC who **violated the terms of a resolution plan** approved twelve months before;

d. a corporate debtor against which a **liquidation order** has been made.

[SM 193–194]

### TIME LIMIT (s.12) · ASKED 3 TIMES AS AN MCQ

- The CIRP must be completed within **180 days from the date of admission**. [SM 196]
- The RP applies for an extension if the CoC so resolves by **66% of the voting shares** (Dec'24 MCQ). The NCLT may extend by up to **90 days**. [SM 196]
- So **180 + 90 = 270 days** with extension (Dec'25 and Jun'26 MCQ answer); the outer limit is **330** (see ⚠).
- Moratorium period in the SM chart: "180 or 270 days" (fill-in 4: maximum **270**). [SM 193, SM 215–216]

**s.12A WITHDRAWAL · 2026 AMENDMENT (DEC'26 SUPPLEMENTARY)**

An admitted application may be **withdrawn** only with the approval of **90%** of the CoC's voting share, subject to the amended conditions. Where **several applications** are pending against the same debtor, the **first application's date** is the initiation date. In force from **26 May 2026**. [Supp Dec'26 p.4]

| Route | Financial creditor (s.7) | Operational creditor (s.8–9) | Corporate applicant (s.10) |
|---|---|---|---|
| before filing | none; can file alone or jointly; for a class (e.g. allottees), at least **100** or **10%** of the class, whichever is less [SM 194] | **demand notice** or copy of invoice; the debtor has **10 days** to pay or point to a dispute (suit or arbitration) [SM 195] | books of account; proposed IRP; a **special resolution** or approval of **3/4th** of partners [SM 196] |
| the application | record of default + name of the proposed RP [SM 194] | prescribed form with s.9(3) documents; may propose an IRP | prescribed form |
| NCLT decides | within **14 days**; checks default from an **information utility** or other evidence [SM 194–195] | within **14 days**; **rejects if a dispute notice was received**; it does not judge whether the dispute is genuine [SM 195–196] | within **14 days**: admit if complete [SM 196] |
| rejection | no default; incomplete; disciplinary proceedings against the proposed RP; **7 days** to rectify first [SM 195] | incomplete; debt paid; no demand notice; dispute received; proceedings against the IRP [SM 195–196] | incomplete; **7 days** to rectify first [SM 196] |

In every route the **CIRP commences on the date of admission**. Defaults in the year from **25 March 2020** (COVID) are not counted. [SM 195–196]

## s.13–18 Moratorium, public announcement, interim resolution professional · Jun'25 Q2(b)

### ON ADMISSION THE NCLT SHALL

(a) **declare a moratorium**; (b) cause a **public announcement** of the CIRP and **call for claims**; (c) **appoint an IRP**. The announcement is made immediately after the IRP is appointed. [SM 196–197]

**Moratorium (s.14) prohibits:** (a) **suits** and proceedings against the debtor, including execution of decrees; (b) the debtor **transferring or encumbering** its assets; (c) any action to **enforce a security interest**, including under SARFAESI; (d) an owner or lessor **recovering property** occupied by the debtor. **Essential supplies** may not be cut off. [SM 197]

**Does not apply to:** transactions the CG notifies with a financial-sector regulator; a **surety** in a contract of guarantee to the debtor. **Lasts** from the order until the CIRP ends, or earlier on **plan approval or a liquidation order**; the period is excluded from limitation. [SM 197] *Never asked long: a fresh question is likely some day.*

### MANAGEMENT BY THE IRP (s.17) · THE JUN'25 ANSWER

- SM WORDS From the date of appointment of the IRP, the **management of the affairs** of the corporate debtor **shall vest in the IRP**. [SM 198]
- The **powers of the board** or partners **stand suspended** and are exercised by the IRP. [SM 198]
- **Officers and managers report to the IRP** and give access to documents and records. [SM 198]
- **Banks** holding the debtor's accounts act on the IRP's instructions and give him all information. [SM 198]
- The IRP protects and preserves the property and runs the debtor **as a going concern** (SM MCQ 6): appoints professionals, makes contracts, raises **interim finance**, instructs employees (s.20). [SM 198]
- **Authority (s.17(2)):** acts and signs in the debtor's name; accesses its records in **information utilities**, with Government authorities and the **statutory auditors**; complies with laws on its behalf. [SM 198]

### DUTIES OF THE IRP (s.18)

a. **collect information** on assets, finances and operations: business operations and payments for the previous **two years**; assets and liabilities as on the initiation date
b. **receive and collate claims**
c. **constitute the committee of creditors**
d. **monitor the assets** and manage operations until the CoC appoints an RP
e. file information with the **information utility** if necessary
f. take **control and custody of assets** owned by the debtor
g. other duties specified by the Board

[SM 198–199]

The personnel and promoters must cooperate; if not, the IRP applies to the **NCLT for directions**. [SM 199]

### APPOINTING THE IRP · THE RP

- The NCLT appoints the IRP on the **insolvency commencement date**; the IP proposed by the applicant is appointed if **no disciplinary proceedings** are pending against him. [SM 197]
- **First CoC meeting within 7 days** of its constitution (SM MCQ 7): by **66%** of voting share the CoC confirms the IRP as RP or **replaces** him (the Board must confirm the new name). [SM 199]
- The RP may later be replaced by **66%** (s.27; SM MCQ 8) with NCLT approval after the IBBI clears the name. [SM 199]
- The RP **conducts the entire CIRP** and manages operations, with the IRP's powers and duties. [SM 200]

## s.21–28 Committee of creditors and the RP · Dec'24 Q4(a), ICMAI MQP Q5(b)

### COMMITTEE OF CREDITORS (s.21, 24)

- Constituted by the IRP after collating claims; comprises **all financial creditors**. A **related-party FC** has **no right of representation, participation or voting**. [SM 199]
- A creditor who is both FC and OC sits **as an FC to the extent of the financial debt**. [SM 199]
- Ordinary decisions: at least **51%** of voting share. The CoC may demand financial information; the RP gives it within **7 days**. [SM 199]
- **Meetings (s.24)**: in person or electronic, run by the RP. Notice to (a) CoC members, (b) the **suspended directors** or partners, (c) **OCs** whose dues are at least **10%** of the debt. Directors and one OC representative may attend but have **no vote**. A member may be represented by another IP. [SM 200]

### s.28 · NEEDS THE CoC'S PRIOR APPROVAL BY 66% (DEC'24 Q4(a))

a. raise any **interim finance**
b. create any **security interest** over assets
c. change the **capital structure**
d. record a change in **ownership interest**
e. instruct banks on a **debit transaction**
f. any **related party transaction**
g. amend **constitutional documents**
h. **delegate** its authority
i. dispose of or permit disposal of **shares** to third parties
j. change the **management** of the debtor or its subsidiary
k. transfer rights or debts under **material contracts** outside the ordinary course
l. change the appointment or terms of **personnel** specified by the CoC
m. change the **statutory or internal auditors**
n. invite prospective **resolution applicants** meeting CoC criteria

[SM 200–201]

**SM WORDS** Without the prior approval of the CoC, with **66% voting in favour**, the action **will be invalid** and action may be taken against the IP. [SM 200]

## s.29–31 Resolution plan: who may bid, contents, approval · Dec'25 Q5(b), Jun'25 MCQ

### s.29A · WHO CANNOT SUBMIT A PLAN

A person, or anyone acting jointly or in concert with him, who:

a. is an **undischarged insolvent**
b. is a **wilful defaulter**
c. has an account classified as an **NPA** for at least **one year** before the CIRP began (eligible if all overdue amounts with interest are paid before submitting the plan; not applied to the applicant for **three years** after the plan's approval)
d. was **convicted**: imprisonment of **two years** under the 12th Schedule offences, or **7 years** under any law
e. is **disqualified as a director** under the Companies Act (SM T/F 2)
f. is **barred by SEBI** from the securities market
g. was promoter or in management of a debtor where a **preferential, undervalued, extortionate or fraudulent** transaction took place and the AA made an order
h. gave a **guarantee** to a creditor of the debtor
i. has a similar disability **abroad**
j. has a **connected person** ineligible under (a)–(i)

[SM 194]

*Jun'25 MCQ (= SM MCQ 19): 1, 2 and 3 all disqualify, so the answer is (A).*

### FROM INFORMATION MEMORANDUM TO APPROVAL

1. **Information memorandum** (s.29): prepared by the RP. Applicants get access to relevant information and undertake **confidentiality**, protection of the debtor's **IP**, and no sharing with third parties. [SM 201]
2. The applicant submits the plan with an **affidavit of eligibility under s.29A**. [SM 201] *Dec'26 supplementary: also disclose the **ultimate beneficial owner** and file the **s.32A** affidavit (from 23 Dec 2025).* [Supp Dec'26 p.3]
3. **The plan must provide for** (s.30(2)): (a) **CIRP costs paid first**; (b) OCs paid **not less than** they would get in a **liquidation under s.53**; (c) **management** of the debtor after approval; (d) **implementation and supervision**; (e) **no contravention of law**. [SM 201]
4. **CoC approval**: plans that meet s.30(2) are approved by **66%** of voting share after considering **feasibility and viability**. The applicant may attend but votes only if he is also an FC. [SM 202]
5. **NCLT approval (s.31)**: if satisfied that the CoC-approved plan meets the Code's requirements, it **approves by order**. The plan then **binds** the debtor, its employees, members, creditors and guarantors. If it is **rejected**, **liquidation** follows. [SM 202]

**CIRP costs** [s.5(13)]: interim finance and its cost; the RP's fees; costs of running the business as a going concern; Government costs to facilitate the process. **Interim finance** = financial debt raised by the RP during the CIRP. [SM 202]

**2026 AMENDMENT ON PLANS (DEC'26 SUPPLEMENTARY)**

s.30 now deals with how **dissenting financial creditors** (who do not vote for the plan) are treated in the distribution; "avoidance transactions" are defined to cover preferential, undervalued and extortionate-credit transactions, and fraudulent or wrongful trading. [Supp Dec'26 p.4]

**⚠ FAST-TRACK CIRP (s.55–58): ICMAI MQP Q5(a), NOT IN THE SM**

The SM only mentions it (SM 203). From the Act: **who**: debtors notified by the CG, which in June 2017 notified (a) **small companies** under the Companies Act, (b) **start-ups** (other than partnership firms), and (c) **unlisted companies with total assets up to ₹1 crore**. **Time**: **90 days** from the insolvency commencement date. The RP may seek an extension if the CoC resolves by **66%**, and the NCLT may extend **once**, by up to **45 days**. The CIRP procedure applies otherwise; if there is no plan in time → liquidation.

## 2.3 Liquidation of a corporate person · never asked; s.53 amended by the 2026 Act

**WHEN THE NCLT ORDERS LIQUIDATION (s.33)**

- **No resolution plan** received within the CIRP period (s.12) or the fast-track period (s.56); or the plan is **rejected** under s.31. [SM 203]
- The CoC resolves by **66%** to liquidate, at any time before the plan is confirmed. [SM 203]
- The debtor **contravenes an approved plan** (on the application of an affected person). [SM 203]
- Then: liquidation order · public announcement · order sent to the registering authority. **No suit** by or against the debtor, except by the liquidator with NCLT approval. [SM 203]
- **Liquidator**: the RP acts, on written consent, unless replaced; the powers of the board and KMP **vest in the liquidator**. [SM 203–204]
- **Powers**: verify claims; take custody of assets; value, protect and sell them (not to persons ineligible under s.29A); carry on the business for a beneficial liquidation; sue and defend; investigate undervalued or preferential transactions; distribute proceeds. [SM 204]
- **Claims**: collected within **30 days** of the liquidation commencement; decision communicated in **7 days**; appeal within **14 days**. [SM 206]

**LIQUIDATION ESTATE (s.36) (SM SHORT ESSAY c)**

Held by the liquidator **as a fiduciary** for all creditors. **In:** assets the debtor owns (incl. shares in subsidiaries), encumbered assets, tangible and intangible assets, assets recovered through avoidance proceedings, assets on which a secured creditor **relinquished** security, and the proceeds. [SM 204–205]

**Out:** third-party assets in its possession (**trust**, **bailment**, **PF, pension and gratuity** dues of workmen and employees); collateral of financial service providers subject to netting; **personal assets of shareholders or partners**; assets of **Indian or foreign subsidiaries**. [SM 205]

**Avoidance transactions: preferential** (s.43: a transfer that puts a creditor or guarantor in a better position than under s.53); **undervalued** (s.45: gifts, or consideration significantly below market value), looked back **one year**, or **2 years** for related parties (s.46); **defrauding creditors** (s.49: to keep assets out of creditors' reach). The NCLT may **reverse** them. [SM 206–207]

**Secured creditor (s.52):** (a) **relinquish** the security to the estate and share under s.53; or (b) **realise** it himself and hand any **surplus** to the liquidator. [SM 207–208]

| Rank | Distribution waterfall (s.53) |
|---|---|
| 1 | **CIRP costs and liquidation costs**, paid in full [SM 208] |
| 2 | equally: **workmen's dues for 24 months** before the liquidation commencement date, and debts of **secured creditors who relinquished** their security [SM 208] |
| 3 | **wages and dues of other employees for 12 months** [SM 208] |
| 4 | **financial debts of unsecured creditors** [SM 208] |
| 5 | equally: **Government dues for 2 years**, and the **unpaid balance of secured creditors who enforced** their security [SM 208] |
| 6 | **any remaining debts and dues** ⚠ the SM skips this clause (f) and goes from (e) to (g) |
| 7–8 | **preference shareholders**, then **equity shareholders or partners** [SM 208] |

**Dissolution (s.54)**: when the assets are fully liquidated, the liquidator applies; the NCLT orders dissolution from the date of the order; the order goes to the registering authority within **7 days**. [SM 208] *Dec'26 supplementary: s.53 distribution "clarified" by the 2026 Act (no detail given).* [Supp Dec'26 p.4]

## 2.4 Personal insolvency (individuals and partnership firms) · Dec'24 MCQ came from here

- A creditor (alone or jointly) applies for **bankruptcy** within **3 months** of an order under s.100(4) (defrauding a creditor), s.115(2) (repayment plan rejected) or s.118(3) (repayment plan not satisfied). The application **cannot be withdrawn** without the AA's permission. [SM 209]
- **Interim moratorium** from the date of application: all litigation is stayed. [SM 209]
- **SM WORDS** The IP proposed shall be continued or rejected by the AA based on information sent by the Board. **If none is proposed, the AA requests a nomination within 7 days and the Board nominates within 10 days** (Dec'24 MCQ: option A). A CoC with **75%** may replace the bankruptcy trustee. [SM 209]
- Claims: notice within **10 days**; registration within **7 days** of the public notice; list of creditors in **14 days**; creditors' meeting within **21 days**. Bankruptcy order within **14 days**; secured creditors must act within **30 days**. [SM 209–210]
- **The bankrupt** may not be appointed a trustee or public servant or be elected to a local authority; may not act as a **director** or promote companies; must **disclose** the bankruptcy in all dealings; and needs permission to **travel overseas** (SM MCQ 10). [SM 210]
- **Adjudicating Authority = Debt Recovery Tribunal** (DRT) where the debtor resides or works (SM MCQ 9). Civil courts have no jurisdiction. [SM 210]
- Appeal to the **DRAT**, then to the **Supreme Court** on questions of law. The SM says "within 15 days" for the DRAT appeal. [SM 210] ⚠ The Act's s.181 gives 30 days, plus up to 15 more for sufficient cause.

## M Model answers

**MODEL ANSWER 1 · CIRP BY A FINANCIAL CREDITOR: ROLE OF THE NCLT, RP DUTIES, PLAN (JUN'26 Q5(b), PTP Q5(a)) · 7 MARKS**

1. **Initiation (s.7):** on a default, ABC Ltd.'s financial creditors, alone or jointly, apply to the **NCLT** with the **record of default** and the name of a proposed RP. [SM 194]
2. **Role of the NCLT:** within **14 days** it ascertains the default from an information utility or other evidence; it admits the application, or rejects it (no default, incomplete, or disciplinary proceedings against the proposed RP) after giving **7 days** to rectify. The CIRP **commences on admission**. It then declares a **moratorium**, orders a **public announcement** and appoints the **IRP**. [SM 194–197]
3. **IRP/RP:** management **vests in the IRP** and the board is suspended; he collects information and claims, **constitutes the CoC** and runs the company **as a going concern**. The CoC confirms or replaces him as RP by **66%**. The RP prepares the **information memorandum**, invites resolution applicants, and needs CoC approval for **s.28** actions. [SM 198–201]
4. **Plan:** applicants (not barred by **s.29A**) submit plans; the RP puts compliant plans to the CoC, which approves by **66%**; the NCLT approves under **s.31**, after which the plan **binds all stakeholders** and is implemented under its supervision terms. Rejection or no plan in **180 (+90) days → liquidation**. [SM 196, SM 201–202]

**MODEL ANSWER 2 · NBFC LENDER CASE (ICMAI PTP Q5(b))**

**Facts:** an NBFC lent money at interest to a company, which defaulted. (1) **Creditor type:** money **borrowed against payment of interest** is a **financial debt**, so the NBFC is a **financial creditor** [s.5(7), 5(8)(a)]. [SM 189] (2) **Where:** it files under **s.7** before the **NCLT** (the AA for companies), with the record of default; no demand notice is needed. (3) **IRP:** the IP it proposes is appointed IRP if no disciplinary proceedings are pending. (4) **Time: 180 days** from admission, extendable once by up to **90 days** on a **66%** CoC resolution. [SM 190, SM 194, SM 196–197]

**MODEL ANSWER 3 · APPROVAL OF A RESOLUTION PLAN BY THE NCLT (DEC'25 Q5(b))**

Write steps 2–5 of "From information memorandum to approval" above, in order: s.29A affidavit → s.30(2) contents (CIRP costs first; OCs at least their liquidation value; management; implementation and supervision; lawful) → CoC approval by **66%** on feasibility and viability → RP submits it to the NCLT → the NCLT approves **if satisfied that it meets the Code → binding** on the debtor, employees, members, creditors and guarantors → if rejected, **liquidation**. Add the 2026 changes: beneficial-owner disclosure and the s.32A affidavit. [SM 201–202] [Supp Dec'26 p.3]

**Other past long questions are answered word for word by the SM boxes above:** s.11 list (Jun'24 Q2(b)) · IRP management (Jun'25 Q2(b)) · s.28 list + 66% (Dec'24 Q4(a)) · applicability (Jun'23 Q3(d)).

### The SM's own exercise for the IBC (SM 211–216)

| | | | |
|---|---|---|---|
| 1 Code passed in | **2016** | 11 CIRP with extension ★★ | **270 days** ⚠ (SM key says 180) |
| 2 applies to companies, LLPs, firms | **all of the above** | 12 not applicable to ★ | **financial service providers** |
| 3 applies to banks, insurers, ARCs | **none of the above** | 13 laws replaced | **all the above** |
| 4 security interest in his favour | **secured creditor** | 14 IBBI's court powers ★ | **civil court** |
| 5 normal CIRP time ★ | **180 days** | 15 insolvency professional agency | **ICMAI** (key) ⚠ |
| 6 RP runs the company as a | **going concern** | 16 regulator | **IBBI** |
| 7 first CoC meeting within | **7 days** | 17 related party | **all of the above** |
| 8 RP replaced by | **66%** | 18 "person" includes | **all of the above** |
| 9 AA for personal insolvency | **DRT** | 19 s.29A ★ | **all of the above** |
| 10 the bankrupt shall | **all or any of the above** ⚠ (SM key says a) | | |

⚠ MCQ 11: the SM key (c) 180 days ignores the extension; Dec'25 and Jun'26 gave 270 as an option and that is the answer. MCQ 10: all four restrictions are in the SM text, so (d). MCQ 15: the key is (a); in fact each of the three institutes has set up its own IPA, so "all of them" is defensible.

**True/False:** CIRP in 180 days from the application **T** (strictly, from admission) · a disqualified director cannot be a resolution applicant **T** · secured creditor definition **T** · NCLT = "National Corporate Law Tribunal" **F** (Company) · corporate applicant = corporate creditor **F**. **Fill-ins:** assignee is also a **financial** creditor · the process ends **180** days from commencement · legal suspension of repayment = **moratorium** · maximum moratorium **270** days · plan approval: SM key **75**% ⚠ (the SM's own text and the current law say **66%**; write 66) · process period **180** days · NCLT decides in **14** days · extension up to **90** days.

## R Revision: numbers

| Rule | Number | Rule | Number |
|---|---|---|---|
| minimum default (SM / now) | ₹1 lakh / ₹1 crore | CoC ordinary decisions | 51% |
| NCLT admits or rejects within | 14 days | RP appoint / replace; s.28; plan; extension; liquidate | 66% |
| time to rectify defects | 7 days | s.12A withdrawal (supp) | 90% |
| OC: debtor's reply to demand notice | 10 days | OCs at CoC meetings if dues ≥ | 10% |
| CIRP / extension / with extension | 180 / 90 / 270 days | related party: shareholding / votes | > 2% / > 20% |
| outer limit (SM / Act) | 360 / 330 days | s.29A: NPA / conviction | 1 yr / 2 or 7 yrs |
| first CoC meeting | 7 days | s.11 bar after a CIRP or plan | 12 months |
| info to CoC / IRP records cover | 7 days / 2 years | workmen / employees' dues (s.53) | 24 / 12 months |
| liquidation claims / decision / appeal | 30 / 7 / 14 days | Govt dues (s.53) | 2 years |
| undervalued look-back / related | 1 yr / 2 yrs | personal: nominate IP (AA / Board) | 7 / 10 days |
| fast track / extension (Act) | 90 / 45 days | bankruptcy application within | 3 months |

# Module 3 · Corporate Governance, CSR and Sustainability P13 ·

## Section A · topics 3.1–3.5

SM pp. 219–252 (+ the CSR law on SM 60 and 127). **93 marks in 7 papers. CSR has come in every paper**; governance and sustainability supply **MCQs (viii) and (ix)** almost every time.

| Topic | J23 | D23 | J24 | D24 | J25 | D25 | J26 | Total |
|---|---|---|---|---|---|---|---|---|
| **3.4** CSR (law + practice + NGRBC) | 12 | 7 | 7 | 7 | 2 | 7 | 7 | **49** |
| **3.5** Sustainability management | – | – | 9 | 2 | – | 2 | 2 | **15** |
| **3.2** Governance codes in India | – | – | – | 9 | – | 2 | 2 | **13** |
| **3.1** Governance concepts | – | 9 | – | – | – | – | – | **9** |
| **3.3** Governance in family business | – | – | – | – | 7 | – | – | **7** |

**HOW IT IS EXAMINED: THE SM'S OWN EXERCISE AND SOLVED CASE ARE THE QUESTION BANK**

- **Jun'26 Q1(viii)** = SM MCQ 15 (Kumar Mangalam Birla, Clause 49A) · **Dec'25 and Jun'26 Q1(ix)** = SM MCQ 4 (paddy is not sustainable development) · **Dec'25 Q1(viii)** = SM MCQ 23 (CG ratings by credit rating agencies) · **Jun'25 Q1(vi)** = SM MCQ 20 · **Jun'24 Q1(viii)** = SM MCQs 1/8 (triple bottom line) · ICMAI PTP = SM MCQ 19. **Learn the exercise on the last page.**
- **Jun'23 Q4(b) is the SM's solved Case Study 1 (ABC Tyres)**, and Jun'24 Q4(a) is the same type: a **CSR applicability case from a table of net worth, turnover and profit**. The model answer is in part 6. ⚠ The SM's own solution has a **wrong figure**.
- **Q6(a)** has been a CSR or governance 7-marker in recent papers. **Jun'26 Q6(a) was ICMAI's MQP question word for word.**

**DEC'26: OUR PREDICTION**

- **CSR**: tier A, **7–9 marks**, a 98% chance of appearing. Likely: (1) **implementation methods and problems** (PTP); (2) the **applicability case** from figures (asked 4×); (3) **ZCZP on the Social Stock Exchange, 10% cap** (Dec'26 supplementary, likely as an MCQ); (4) evaluation of CSR projects.
- **MCQs (viii)–(ix):** one governance + one sustainability, a **70%** chance each.

**MAP**

1. Governance concepts (3.1) ★
2. Governance codes, ID code, ratings, LODR reports (3.2) ★★
3. Family business (3.3) ★
4. CSR: law (s.135), activities, implementation, evaluation (3.4) ★★★
5. NVG / NGRBC / SDGs (3.4) ★★
6. Sustainability management, BRSR (3.5) ★★
7. Model answers · SM exercise (all) · numbers

## 3.1 Corporate governance: concepts and issues · Dec'23 Q6(a)

**WHAT IT IS** **Corporate governance (CG)** is how a company's affairs are managed with **fairness, honesty and good practices for the benefit of all stakeholders**, through policies with **checks and balances** between shareholders, directors and auditors. It is "more a **way of business life** than a mere legal compulsion". [SM 219]

| Who | Definition |
|---|---|
| **Milton Friedman** | conducting business in line with shareholders' desire (make as much money as possible) while conforming to the basic rules of society in law and custom [SM 219] |
| **Adrian Cadbury** | SM WORDS "a system by which companies are **directed and controlled**. It has to do with **power and accountability**" [SM 219] |
| **Narayana Murthy Committee** | management accepting the shareholders' **inalienable rights as true owners** and its own role as **trustees**; commitment to values, ethical conduct, separating personal and corporate funds [SM 219] |

**FEATURES (Dec'23 Q6(a): "a statement of the features")**

1. **a tool for transparency**: disclose the state of affairs to every stakeholder at every step; no suppression of material facts
2. **prudent and participative management**
3. **enhancing the value** of the enterprise (money, reputation, goodwill)
4. **accountability** to **all** stakeholders, not one
5. **innovation**
6. **professionalism and specialisation**: no conflict between duty and personal gain; competence
7. **stakeholder recognition**

[SM 220]

**OBJECTIVES · BENEFITS · THEORIES**

**Objectives:** balance stakeholders' conflicting interests · transparent, justifiable policies · an ideal Board composition (LODR) · optimum use of resources · reduce risk through due diligence · build trust and enterprise value. [SM 219–220]

**Benefits:** growth and stability · reputation · better use of funds and resources · long, steady growth · stakeholder confidence · competitive advantage · easier alliances. [SM 221–222]

**Theories: stewardship** (directors as stewards of assets) · **agency** (directors as shareholders' agents) · **stakeholder** (balance all stakeholders) · **trusteeship** (trust placed in directors). [SM 222]

| | Ethics | Management | Corporate governance |
|---|---|---|---|
| foundation | values and principles of the inner self | objects and targets | the method of governing, with ethical values |
| level | all levels | all levels | **top level** (SM MCQ 2) |
| origin | emerges naturally | emerges with the situation | studied and experienced; established guidelines |
| regulation | not important | own rules (law still followed) | **important**: strict compliance |
| focus | – | **results** over method | **method** over results |

[SM 220–221]

**Why CG emerged:** corporate failures (**Xerox, Enron, Global Crossing, WorldCom, MS Shoes, Harshad Mehta, Satyam**) · rise of institutional and retail investors · information in the public domain · regulation · volatility in share prices. [SM 221]

## 3.2 Governance codes, the ID code, CG ratings, LODR reports · Dec'24 Q4(b)

| Committee | Set up by · key recommendations |
|---|---|
| **Cadbury** (the SM says "USA, SEC") | audit committees for listed companies, disclosed in the annual report · external auditor and finance director attend · it reviews the audit scope and the half-yearly and annual FS before the Board · may investigate and take outside advice · its chairman answers at the AGM [SM 223] |
| **Rahul Bajaj** (CII) | India's first formal code: listed companies with turnover **₹100 crore** or paid-up capital **₹20 crore** (whichever is less) to set up audit committees within **2 years**; it assists the Board on financial reporting and interacts with the statutory and internal auditors [SM 223–224] |
| **K R Chandratre** | draft Companies Bill: audit committee where paid-up capital is **₹5 crore**; auditors and the finance head attend **without vote**; reviews internal control and FS; chairman present at the AGM; penalties incl. imprisonment [SM 224] |
| **Kumar Mangalam Birla** (SEBI) → **Clause 49 / 49A** of the listing agreement (SM MCQ 15 = Jun'26 MCQ) | mandatory vs non-mandatory recommendations · FI nominees off Boards (except on default) · **half** the Board independent, **one-third** if the chairman is non-executive · audit committee of at least **3** non-executive directors, majority independent, one with finance knowledge, meeting at least **3 times** a year · remuneration and investor-complaints committees · a director on at most **10** committees, chairing at most **5** · a CG section in the annual report · postal ballot [SM 224–225] |

**Latest CG committee: the Kotak committee** (SM MCQ 6). **Board level**: CG is set by the Act and LODR. **Below Board level**: each company's own code of conduct, service rules, whistle-blower policy, SOPs, run "**top-down**". [SM 225–226]

### SCHEDULE IV: CODE FOR INDEPENDENT DIRECTORS

- **Guidelines:** integrity · objectivity · the company's interest · enough time · no extraneous influence · no abuse of position · avoid losing independence, and inform the Board if it is lost · help implement best CG practice. [SM 226]
- **Role:** independent judgment on strategy, performance, risk, resources and appointments · evaluate the Board and management · monitor performance · check the **integrity of financial information** and controls · protect stakeholders, especially **minority shareholders** · fix pay of executives, KMP and senior management · arbitrate between management and shareholders. [SM 226–227]
- **Duties:** update skills · take outside expert advice at the company's cost · attend Board, committee and general meetings · keep informed · do not obstruct · **report unethical behaviour or fraud** · no disclosure of confidential information or **UPSI**. [SM 227]
- **Appointment:** a balance of skills · **approved by shareholders** · explanatory statement that he is independent · a **letter of appointment** (term, expectations, committees, fiduciary duties, D&O insurance, code of ethics). [SM 227–228]

### CG RATINGS · ESG · LODR COMPLIANCE REPORT

- **CG rating** = an opinion on a company's CG system and its relative standing. Done by **credit rating agencies** (SM MCQ 23 = Dec'25 MCQ). Its **5 uses**: information to stakeholders · an independent assessment for the company · relative standing (domestic and international) · a benchmark for improvement · investors can differentiate. [SM 228]
- **Assessment criteria (16):** Board structure · shareholder rights · accounting · ownership and control · professionalism · disclosures · share price · legal compliance · dividend payout · conflicts · RPTs · risk management · investor, customer and vendor grievances · CSR. [SM 228–229]
- **ESG rating** = Environmental + Social + **Governance** (Board, pay, ownership and control, accounting) ratings, each from key metrics. [SM 229]
- **Reg 27(2) LODR:** a listed entity files a **quarterly compliance report on CG** with the stock exchanges. **Annex I** quarterly · **Annex II** at year-end · **Annex III** 6 months after year-end · **Annex IV half-yearly** (loans, guarantees and comfort letters to promoter-group entities, from FY 2021-22). [SM 229]

⚠ Dec'24 MCQ (vii) asked when Annex IV is filed; the SM says **half-yearly**.

### SUPPLEMENTARIES (SEBI LODR, MCQ MATERIAL)

- **Dec'26:** the **High Value Debt Listed Entity** threshold is raised from **₹1,000 crore to ₹5,000 crore** (from 22 Jan 2026). [Supp Dec'26 p.5]
- **Jun'26 (still applies):** Reg 23 RPTs: a **scale-based materiality** threshold linked to consolidated turnover · **Audit Committee approval for material RPTs of unlisted subsidiaries** · omnibus approvals relied on more · consolidated disclosure formats · the Audit Committee records the rationale and arm's-length nature. [Supp Jun'26 p.5]

## 3.3 Corporate governance in family business · Jun'25 Q3(b)

**IFC definition:** a company where the **voting majority is held by the controlling family**, including founders who intend to pass the business on to their descendants. Family businesses are the world's oldest and most dominant form: more than **70%** of businesses in many countries (Spain about **75%** of businesses, **65%** of GNP; Latin America about **60%** of GNP). In India, about **99%** of corporate houses are owned by individuals or families. [SM 230]

### FEATURES IN INDIA

1. directors and senior managers are family or related
2. coteries form
3. control and ownership dilute with each generation
4. **conflicts of interest** between promoter and company
5. **emotional** decisions
6. a united family sidelines outside directors; a divided family brings confusion, delay and distrust
7. some have clear roles and **succession plans**
8. the chairman's personal image is the company's reputation
9. professionals avoid family firms
10. the death or disability of a senior member → a **leadership crisis**

[SM 230–231]

### EVOLVING CG IN FAMILY COMPANIES (the Jun'25 answer)

i. **separating ownership from management**: promoters stay investors; a professional Board
ii. family members acquire **professional qualifications**
iii. promoters **encourage professionals**
iv. **focus on compliance** to protect reputation and share price
v. **role and leadership clarity** decided at Board level
vi. owners **honour managers' opinions**
vii. the family's social and emotional needs met through **separate trusts or foundations**

**Listed family companies** follow the same codified CG as others; the family's ownership does not change the compliance. *SM MCQ 26: the advantage of a family business is deep industry insight.* [SM 231]

## 3.4 CSR: the law (s.135) · asked in all 7 papers

**WHAT IT IS** **CSR** is business's commitment to operate accountably and contribute to **community welfare, especially the underprivileged**. Its core is **Concern, Care and Share (CCS)**. It is not occasional charity but part of the company's strategy. [SM 232]

### WHO IS COVERED (s.135(1))

In the **immediately preceding financial year**: net worth ≥ **₹500 crore**, OR turnover ≥ **₹1,000 crore**, OR net profit ≥ **₹5 crore**. **Any one test** is enough. [SM 60]

A company that ceases to meet the tests for **3 consecutive financial years** need not have a committee or comply until it meets them again. [SM 127]

**CSR committee: 3 or more directors**, at least **one independent**. Where IDs are not required (unlisted public or private companies), no ID; a private company with **2 directors** has both; a foreign company has the person authorised to accept notices plus a nominee. The Board's report discloses the committee's composition. [SM 60–127]

**No committee needed** if the CSR obligation is up to **₹50 lakh**; the Board does its work (SM fill-in 13; True/False 5). [SM 250–252]

### COMMITTEE FUNCTIONS (Jun'26 Q6(a): "any four")

1. **formulate and recommend a CSR policy** to the Board, showing the Schedule VII activities to be undertaken
2. **recommend the amount** of expenditure
3. **monitor the CSR policy** from time to time
4. institute a **transparent monitoring mechanism** for projects
5. **recommend projects** and modifications to the policy

[SM 60–127]

**Board's duties:** approve the policy after considering the committee's recommendation · **disclose it in the Board's report and on the website** · ensure the activities are undertaken · **spend at least 2%** of the **average net profit of the 3 immediately preceding financial years** (s.198), preferring the **local area**. [SM 60]

**SPEND**
≥ 2% of the 3-year average net profit (s.198) [SM 60]

→

**NOT SPENT, NOT AN ONGOING PROJECT**
reasons in the Board's report; transfer to a **Schedule VII fund** within **6 months** of the year-end [SM 60]

→

**NOT SPENT, ONGOING PROJECT**
transfer within **30 days** of the year-end to a **special (Unspent CSR) account**; spend within the next **3 years** [SM 60]

→

**STILL UNSPENT AFTER 3 YEARS**
transfer to the Schedule VII fund [SM 60]

### DEC'26 SUPPLEMENTARY: ZCZP ON THE SOCIAL STOCK EXCHANGE (EFFECTIVE 27 MAY 2026)

Subscribing to eligible **Zero Coupon Zero Principal (ZCZP)** instruments of eligible **not-for-profit organisations registered on the Social Stock Exchange** is now a **CSR activity** (added to **Schedule VII**). It is capped at **10%** of the company's total CSR expenditure for the year. [Supp Dec'26 p.2]

### ⚠ NOT IN THE SM: PENALTY FOR NOT TRANSFERRING UNSPENT CSR (s.135(7))

Company: **twice the amount** required to be transferred, or **₹1 crore**, whichever is **less**. Every officer in default: **one-tenth** of that amount, or **₹2 lakh**, whichever is less.

# 3.4 CSR in practice: activities, implementation, evaluation · PTP Q6(a), Dec'24 Q5(a)

### WHAT COUNTS (Schedule VII) · WHAT DOES NOT

**Schedule VII** lists the CSR activities: health, nutrition, sanitation, education, skills, inclusive growth, and so on. The list is exhaustive, but the Government says it is to be **interpreted liberally** (SM MCQ 10); e.g. "education" covers training and skills. The beneficiary should ultimately be the **poor and underprivileged** (SM MCQ 13: every CSR activity is for the beneficiary). [SM 236]

**Not CSR:** (a) **publicity** for products · (b) **compliance** with a law or Government order · (c) **employee or family benefits** · (d) infrastructure for **production or distribution** · (e) **political contributions**. *A school for disabled children where 3 of 200 are employees' children still qualifies, as that is incidental (SM MCQ 19, PTP). A donation to an **unrecognised** charity does not qualify (SM MCQ 20, Jun'25).* [SM 236–237]

### IMPLEMENTATION STEPS · PARTNERS

a. **determine the thrust area** (e.g. primary education for poor children)
b. **identify the project** (which school; building, books, meals, scholarships)
c. **evaluate** the project
d. **implement**
e. **monitor**
f. **assess impact**

**Collaborative projects:** with other companies, with Government (PPP), or through specialised agencies. **Implementing agencies:** community organisations, Panchayats, NGOs, institutes, trusts and missions, self-help groups, Government and autonomous bodies, Mahila Mandals. (SM MCQ 7: ideally a section 8 company, trust or society; MCQ 17: a **foreign entity cannot** be an implementing agency.) [SM 237]

### EVALUATION BEFORE SPENDING: DUE DILIGENCE (Dec'24 Q5(a))

**Check:** (1) nature of the project (2) its cost (3) independent or linked (4) collaborative (5) **beneficiaries** (6) technical feasibility (7) financial feasibility (8) implementation time (9) **measurable impact** (10) a monitoring mechanism. [SM 238]

**How:** a team of 2–3 officers inspects the documents and the site with a checklist and writes a structured report. The project report (by the agency or independent professionals) is evaluated. The report with recommendation goes to the **CSR committee → Board** (or a delegated authority). Then an **agreement or MOU**, payment in instalments, monitoring, and a **completion certificate** from an independent CA or chartered engineer. [SM 238]

**Evaluating the agency** (third-party projects): (a) documentation (b) site inspection (c) track record (d) beneficiary feedback (e) sponsors' feedback (f) interviews. The **first step is examining documents** (SM MCQ 12). [SM 239]

### DIRECT vs THIRD-PARTY IMPLEMENTATION (PTP Q6(a))

| | Direct by the company | Through an agency |
|---|---|---|
| plus | flexible · better supervision · quick decisions · little coordination · less cost (SM MCQ 21) | expertise · supervision at site · unbiased · single-point coordination · negotiated cost (SM MCQ 22) |
| minus | manpower · no domain knowledge · **no 80G benefit** · biased · corrective action undefined · negatives undocumented · no local knowledge or language · weak monitoring | may need more supervision · agency may lack domain knowledge · no 80G · biased if also a beneficiary · poor accounting · negatives undocumented · local dominance · weak monitoring |

[SM 239–240]

**Problems in implementation. Internal:** choosing projects · financial mismatch · management not serious · finding the right people · internal references · indecision in the committee. **External:** political and social pressure · uncontrollable roadblocks · an inefficient agency · **diversion, siphoning, fraud**. [SM 240]

**After spending: monitoring** (periodic data, progress, corrective action) and **impact assessment**: preferably by an **independent agency**, focused on impact, done soon after the benefit, data-based; it feeds the next plan. [SM 240–241]

## 3.4 NVG → NGRBC, UNGPs, SDGs · Jun'23 Q2(c), Dec'25 Q6(a)

### THE TIMELINE

- **2011 · NVGs**: the MCA's **National Voluntary Guidelines** on the Social, Environmental and Economic Responsibilities of Business (SM fill-in 10: 2011). [SM 233]
- **2011 · UNGPs**: the UN Human Rights Council endorsed the **Guiding Principles on Business and Human Rights** ("Protect, Respect and Remedy"): the State's duty to protect rights, business's duty to respect them, and access to **remedy** for victims. The UN Working Group urges national action plans. [SM 232–233]
- **2012**: SEBI mandated the **Annual Business Responsibility Report (ABRR)**, based on the NVGs, for the **top 100** listed companies, later the **top 500**. [SM 233]
- **2015 · SDGs**: the UN's 2030 Agenda, **17 goals**, with business as a driver of growth. **Paris Agreement** (Dec 2015; India ratified on **2 Oct 2016**; its commitments are the NDCs). [SM 233]
- **2015** → the NVGs revised to align with the SDGs and UNGPs = **NGRBC** (National Guidelines on Responsible Business Conduct): for **all businesses**, whatever their ownership, size, sector or location, including foreign MNCs; extended to suppliers and partners; the highest governance body oversees them; **9 principles** with core elements; an updated Business Responsibility Reporting Framework (BRRF). [SM 233–235]

### THE 9 NGRBC PRINCIPLES: BUSINESSES SHOULD …

1. conduct and govern themselves with **integrity**, ethically, transparently and accountably
2. provide goods and services in a manner that is **sustainable and safe** (across the life cycle)
3. respect and promote the **well-being of all employees**, including in their value chains
4. respect the interests of, and be responsive to, **all stakeholders**
5. respect and promote **human rights**
6. respect, protect and restore the **environment** (precautionary principle)
7. influence **public and regulatory policy** responsibly and transparently
8. promote **inclusive growth** and equitable development
9. engage with and provide value to **consumers** responsibly

[SM 235–236]

*Jun'23 Q2(c) asked principles 1 and 3. Write the SM's explanation of each: e.g. P1 = ethical behaviour in all operations as the basis of governance, with businesses accountable for adoption, implementation and disclosure; P3 = equity, dignity, well-being and decent work for all employees and the value chain, without discrimination.*

## 3.5 Sustainability management and reporting · Jun'24 Q8(b), postal Q4(a)

### MEANING · TRIPLE BOTTOM LINE (3P)

**Sustainable development**: meeting **present needs without harming the future** (Brundtland Report, "Our Common Future", **1987**). **Sustainable management**: running public affairs and businesses so as to protect resources for the future and stay economically and socially responsible. [SM 242]

| | |
|---|---|
| **Economic** = **Profit** | today's decisions must not impair future living standards |
| **Ecological / environmental** = **Planet** | preserve scarce resources (genetic diversity, water, mines, forests); minimise effluents |
| **Social** = **People** | industry must not harm social security, values or welfare |

[SM 242]

*Jun'24 MCQ: "ergonomic approach" is not one of the three. Dec'25 and Jun'26 MCQ: **paddy cultivation** is not a sustainable development activity (rain-water harvesting, solar and afforestation are).*

### STEPS · AREAS · NEED

**Steps (15):** identify problems → set thrust areas → targets → evaluate and select projects → plan → tools and technology → innovate → schedule → organise → staff → direct → monitor → correct → review. [SM 242–243]

**Areas:** processes that use fewer natural resources · less waste, renewables, recycling, biodegradable packaging · stop deforestation, promote afforestation · effluent treatment · sustainable agriculture · carbon management. [SM 243]

**Need and benefits** (postal Q4(a)): unsustainable firms eventually cannot compete; communities and natural resources need it to last; it links the business with the wider environment; vision becomes practice; planning on sustainable values brings savings and performance; activities kept within the **Earth's carrying capacity**. [SM 243–244]

### SUSTAINABILITY REPORTING: BRR → BRSR (Jun'24 Q8(b), Dec'24 MCQ)

- The UN **Principles for Responsible Investment (PRI)**: about **3,500** investor signatories integrating **ESG** into investment decisions. Most large companies report ESG profiles. [SM 244]
- SEBI prescribed an ESG reporting format in **November 2015**, and revised it in **May 2021** as the **Business Responsibility and Sustainability Report (BRSR)**, reporting performance against the **NGRBC** principles. Each parameter has **essential indicators (mandatory)** and **leadership indicators (voluntary)**. [SM 244]
- **Purpose:** quantified, standard disclosures comparable across companies (for investors) · stakeholder engagement · looking beyond financial figures. [SM 244]
- **Mandatory from FY 2022-23** for the **top 1,000 listed companies** by market capitalisation. [SM 244]

## 6 Model answers

**MODEL ANSWER 1 · CSR APPLICABILITY FROM FIGURES (SM SOLVED CASE 1 = JUN'23 Q4(b) TYPE; JUN'24 Q4(a))**

**SM case:** ABC Tyres Ltd (₹ crore). Turnover 700 / 650 / 920 / 1,010; net worth 402 / 423 / 480 / 530; net profit 14.5 / 15.7 / 16.8 / 18, for 2020-21 to 2023-24. (1) Is CSR applicable? (2) What is the minimum budget for 2024-25? (3) Is a committee needed? [SM 251]

1. **Applicable?** s.135(1) applies if, in the **preceding** year (2023-24), net worth ≥ ₹500 cr, turnover ≥ ₹1,000 cr, or net profit ≥ ₹5 cr. In 2023-24 **all three** are met (530, 1,010, 18), so **CSR applies**.
2. **Minimum budget for 2024-25** = 2% of the average net profit (s.198) of the **3 immediately preceding years** (2021-22 to 2023-24) = 2% × (15.7 + 16.8 + 18) ÷ 3 = 2% × 16.83 = **₹0.3367 crore ≈ ₹33.67 lakh**.
3. **Committee?** The company is covered, but its obligation (₹33.67 lakh) is **below ₹50 lakh**, so **strictly no committee is required**; the Board can discharge the committee's functions. Answer: "covered by s.135; no committee required as the obligation does not exceed ₹50 lakh". The SM's solution says "Yes, required".

**⚠ THE SM'S SOLUTION HAS TWO SLIPS**

It prints the budget as "**₹3.37 lakhs**". 2% of ₹16.83 crore is **₹33.67 lakh** (a decimal slip). It also says a committee is required, though its own exercise answer (fill-in 13) says no committee is needed when the obligation is up to **₹50 lakh**. In the exam, show the working; the examiner marks the method. [SM 251–252]

**Jun'24 RR Ltd (same method):** 2022-23: net worth 503 (≥ 500) and net profit 8.9 (≥ 5) → **covered** for 2023-24. Budget = 2% × (6.9 + 7.9 + 8.9) ÷ 3 = 2% × 7.9 = **₹15.8 lakh** → below ₹50 lakh → **no CSR committee required**. Then state the other obligations (policy, Board's report, website, unspent transfers).

**MODEL ANSWER 2 · CSR COMMITTEE: APPLICABILITY AND FOUR FUNCTIONS (JUN'26 Q6(a) = ICMAI MQP Q6(a) VERBATIM) · 7 MARKS**

1. **Applicability (s.135(1)):** a company with net worth ≥ **₹500 crore**, or turnover ≥ **₹1,000 crore**, or net profit ≥ **₹5 crore** in the immediately preceding financial year must constitute a **CSR Committee of the Board**. [SM 60]
2. **Composition: 3 or more directors, at least one independent**. Where no ID is required, two or more directors; a private company with 2 directors, both; a foreign company, its authorised person and a nominee. Disclosed in the Board's report. [SM 60–127]
3. **Exemptions:** no committee where the obligation is **up to ₹50 lakh** (the Board acts); and none after the company has **ceased to meet the tests for 3 consecutive years**. [SM 127–252]
4. **Four functions:** (i) **formulate and recommend a CSR policy** showing the Schedule VII activities; (ii) **recommend the amount** of expenditure; (iii) **monitor the policy** from time to time; (iv) set up a **transparent monitoring mechanism** for projects and recommend projects to the Board. [SM 60–127]
5. **Board's role (to round off):** approve and disclose the policy, ensure 2% of the 3-year average profit is spent, and transfer unspent amounts (6 months / 30 days rules). [SM 60]

## Q The SM's own exercise for Module 3, with answers (SM 245–252)

| | | | |
|---|---|---|---|
| 1 3 Ps of the triple bottom line | **planet, people, profit** | 14 ongoing-project CSR money spent within | **3 years** |
| 2 CG is most relevant at | **top level** | 15 Clause 49A based on ★ | **Kumar Mangalam Birla** |
| 3 undesirable practice | **using secret information from unfair sources** | 16 CG is close to | **ethical conduct of business** |
| 4 not sustainable development ★ | **paddy cultivation** | 17 a foreign entity cannot be | **CSR implementing agency** |
| 5 CG practices in India are almost | **regulated** | 18 why companies fail at CG | **narrow promoters, money, unhealthy competition: any** |
| 6 latest CG committee | **Kotak** | 19 school with 3 employees' children ★ | **still CSR (incidental)** |
| 7 ideal implementing agency | **s.8 company, trust or society: one of them** | 20 does not qualify as CSR ★ | **donation to an unrecognised charity** |
| 8 economic approach relates to | **profit** | 21 / 22 advantages, direct / third party | **all of the above / all of the above** |
| 9 CG is more about | **a fair method of managing** | 23 CG ratings by ★ | **credit rating agencies** |
| 10 Schedule VII to be | **liberally interpreted** | 24 audit committee interacts with | **statutory and internal auditors** |
| 11 CG balances the interests of | **all stakeholders** | 25 audit committee recommendation | **if not accepted, Board records reasons** |
| 12 first step in evaluating an agency | **examining documents** | 26 family business advantage | **deep industry insight** |
| 13 every CSR activity is for the | **beneficiary** | | |

| True / False | |
|---|---|
| most CG provisions for listed companies are in LODR | **T** |
| stakeholders = shareholders only | **F** |
| CSR committee chairman must be an ID | **F** |
| signing the code of conduct is optional | **F** |
| a ₹90 lakh CSR budget needs a committee | **T** |

| Fill in the blanks | |
|---|---|
| CG is practised at … level | **top** |
| CSR turnover test, ₹ crore | **1,000** |
| committee in the listing agreement / CEO certificate on | **KM Birla / code of conduct** |
| ABRR = Annual … Responsibility Report | **Business** |
| max committees per director / remuneration schedule | **10 / V** |
| PRI / SDG | **Principles of Responsible Investment / Sustainable Development Goals** |
| voluntary CSR guidelines / CSR schedule | **2011 / VII** |
| no CSR committee if the budget is up to | **₹50 lakh** |

**Numbers:** CSR ₹500 cr / ₹1,000 cr / ₹5 cr · 2% of the 3-year average · committee 3 (1 ID) · none up to ₹50 lakh · unspent 6 months / 30 days / 3 years · ZCZP cap 10% · stop after 3 years out of the tests · ABRR top 100 → 500 · BRSR top 1,000 from 2022-23 · SDGs 17 (2015) · NVGs 2011 · Brundtland 1987 · PRI 3,500 · KMB: half IDs / one-third, 10 / 5 committees, audit committee ≥ 3, meets 3× · HVDLE ₹5,000 cr.

# Module 4 · SEBI Laws and Regulations P13 · Section B (Economic Laws)

SM pp. 255–272: 13 pages of text + 3 of exercise. A long question in every paper from a short module, so prepare all 3 topics for 7 marks.

| Topic | Law | What it covers | SM pages |
|---|---|---|---|
| **4.1** Raising Finance from Capital Markets – IPO | SEBI (ICDR) Regulations, 2018 | who cannot make a public issue; IPO entry tests; pricing; promoters' contribution & lock-in; book building | 257–260 |
| **4.2** Insider Trading | SEBI (PIT) Regulations, 2015 | insider, connected person, UPSI; ban on communicating & trading; trading plan; disclosures; two codes; institutional mechanism | 261–264 |
| **4.3** Takeover Code | SEBI (SAST) Regulations, 2011 | definitions; kinds of takeover; disclosures; open-offer triggers (25% / 5%); open-offer timeline; obligations; exemptions | 265–269 |

### Marks in the last 7 papers [question bank, P13 analysis 5 Oct]

| Topic | Jun'23 | Dec'23 | Jun'24 | Dec'24 | Jun'25 | Dec'25 | Jun'26 |
|---|---|---|---|---|---|---|---|
| 4.1 IPO (+ SEBI basics) | – | 2 + **7** | 2 | 2 | 2 | **7** | 2 |
| 4.2 Insider trading | **8** | – | **7** case | **7** | – | – | 2 + **7** |
| 4.3 Takeover code | – | – | 2 | – | **7** | – | 2 |
| **Module total** | **8** | **9** | **11** | **9** | **9** | **7** | **13** |

**Bold** = long question (7–8 marks): one came in **all 7 papers**, plus 1–3 MCQs of 2 marks. The law in the long question rotates: IPO (Dec'23, Dec'25), insider trading (Jun'23, Jun'24, Dec'24, Jun'26), takeover (Jun'25).

**HOW THIS MODULE IS EXAMINED: THE EXAM COPIES THE STUDY MATERIAL**

- **Dec'23 Q7(a)** is the first line of SM 4.1.1, word for word. **Jun'26 Q1(x)** is the SM's definition of book building. **Jun'26 Q1(xii)** is the SM's definition of conglomerate takeover.
- **Dec'24 Q1(ix) and Jun'25 Q1(ix)** are MCQ 7 of the SM's own exercise. **Jun'24 Q1(iv) and Q1(xi)** are its fill-in-the-blanks 3 and 5. **Dec'23 Q1(v)** is fill-in-the-blank 1. So **the exercise on SM 270–272 is a question bank**, and it is on the last page of this pack.
- ICMAI's own model answers (MQP and PTP Q7(a), 2026) are the SM paragraphs copied out. **Write the SM's points in the SM's order.** Lines tagged SM WORDS are worth learning word for word.

**DEC'26: OUR PREDICTION (A PREDICTION, NOT A PROMISE)**

| Slot | Most likely | Chance |
|---|---|---|
| Q7(a), 7 marks | 4.3 Takeover: kinds + obligations + offer price | 35% |
| | 4.1 IPO eligibility (both December papers asked it) | 35% |
| | 4.2 Insider trading (just asked in Jun'26) | 20% |
| Q1 MCQs (x)–(xii) | IPO · Takeover · Insider | 80 · 60 · 40% |

How far to trust it: our P13 method covered 80% of the real Jun'26 marks in the backtest, and 86% with ICMAI's practice papers added.

**STUDY ORDER AND WHAT TO LEARN**

1. **4.3 Takeover** ★★★. It was in ICMAI's MQP and PTP, and was amended for Dec'26 (independent registered valuer).
2. **4.1 IPO** ★★★. Learn the 10 "cannot issue" conditions, the 3 entry tests and the numbers.
3. **4.2 Insider** ★★. Learn the definitions, the two bans and the 5-point institutional mechanism.
4. Then the **revision sheet** (numbers, plus the SM exercise and its answers) before every mock.

**SEBI ITSELF: FROM THE SM EXERCISE, ASKED AS AN MCQ IN DEC'24 AND JUN'25**

SM WORDS The Preamble sets up SEBI to **protect the interests of investors** in securities, **promote the development** of the securities market and **regulate** it ("all of the above"). SEBI has **three functions rolled into one body: quasi-legislative, quasi-judicial, quasi-executive**. "Quasi-official" is **not** one of them. [SM 270–271]

# 4.1 Raising Finance from Capital Markets – IPO (SEBI ICDR)

**WHAT IT IS** SEBI's ICDR rules decide who may raise money from the public and what an IPO company must prove first: profits, assets and net worth, or else selling mostly to big institutions. They also set the issue price, how much the promoters must put in and lock in, and how the shares are divided among investor groups (book building). [SM 257–260]

## 4.1.1 When an issuer cannot make a public or rights issue [SM 257]

**SM WORDS** "An issuer cannot make a public issue or rights issue of equity shares and convertible securities under the following conditions:" *(This line is Dec'23 Q7(a), word for word.)*

| Group | Condition (SM order) |
|---|---|
| **People** | **(a)** the issuer, any promoter, promoter group, director or selling shareholder is **debarred by SEBI** from the capital market, or any company they are linked to is debarred · **(h)** for a public issue of equity: the issuer, a promoter or a director is a **wilful defaulter** [SM 257] |
| **Paperwork** | **(b)** no application to stock exchange(s) for **"in-principle" listing approval**, and no **designated stock exchange** chosen. For an IPO, at least one recognised exchange must have **nationwide trading terminals** · **(c)** no agreement with a **depository** for dematerialisation · **(d)** existing **partly paid-up shares** not yet fully paid up or forfeited · **(f)** promoters' holding not in **demat form** before the offer document is filed [SM 257] |
| **Money & numbers** | **(e)** firm arrangements of finance, through verifiable means, are not in place for **75%** of the stated means of finance. Issue money and existing internal accruals are excluded from this. · **(g)** money for **general corporate purposes** must not exceed **25%** of the amount raised · **(i)** the issue stays open for at least **3 days** and at most **10 days** · **(j) minimum subscription 90%** of the issue size, or the application money is refunded within **15 days** of closure [SM 257] |

**MEMORY HOOK**

Three groups: **People** (debarred, wilful defaulter) · **Paperwork** (listing, depository, partly-paid, promoter demat) · **Money** (75, 25, 3–10, 90/15). In the exam, write them in the SM order (a)–(j).

## 4.1.2 Intermediaries the issuer must appoint [SM 257–258]

- One or more **merchant bankers**, at least one of them the **lead merchant banker**. If there are several, each one's duties are fixed beforehand and disclosed in the offer document.
- Other **SEBI-registered intermediaries**, chosen with the lead merchant banker.
- Book-built issue: **syndicate member(s)**. Any other issue: **bankers to the issue** at various centres.
- A **Registrar to the issue** registered with SEBI, with connectivity to all depositories.
- A **compliance officer**, who monitors compliance with securities laws and handles investor grievances. *SM exercise MCQ 2: at IPO the issuer must have a "designated compliance officer".*

## 4.1.3 Entry tests for an IPO: which route? [SM 258]

**ROUTE 1: TRACK RECORD (all four tests)**

1. **Net tangible assets ≥ ₹3 crore** in each of the preceding **3 years** (12 months each). Not more than **50%** may be monetary assets; if more, the excess must be firmly committed to the business. The 50% limit does not apply if the IPO is entirely an **offer for sale**. [SM 258]
2. **Average pre-tax operating profit ≥ ₹15 crore**, restated and consolidated, in the **3 most profitable of the last 5 years**. [SM 258]
3. **Net worth ≥ ₹1 crore** in each of the preceding **3 full years**. [SM 258]
4. If the name was changed within the last **1 year**: at least **50%** of the last year's revenue came from the activity the new name shows. [SM 258]

**ROUTE 2: FAILS ANY TEST → QIB ROUTE**

The IPO is still allowed if the issue is made **through book building** and the issuer allots **at least 75% of the net offer to qualified institutional buyers (QIBs)**. If it fails to do so, it must **refund** the full subscription. [SM 258]

**Why these tests exist** (Dec'25 asked "why"): only companies with real assets, a profit record and positive net worth should take money from small investors. A company without that record must sell mainly to QIBs, the informed investors who can judge the risk. This protects retail investors, which is SEBI's first purpose. (This is reasoning built on the SM rules; the SM itself gives no "why".)

**Other IPO conditions** [SM 258]: an IPO of **convertible debt instruments** is allowed without first listing equity, if there has been no default in principal or interest for **6 months** · there must be at least **1,000** prospective allottees · no IPO while **outstanding convertible securities** or options to receive shares exist · if the issue is above **₹100 crore**, a bank or PFI monitors the use of the money and reports **quarterly** until **95%** is used · IPO **grading** by SEBI-registered credit rating agencies is optional.

### 4.1.4 Pricing and differential pricing [SM 258–259]

- The price is fixed with the **lead merchant banker** or through **book building**. The offer document may give a **price or price band**; the red herring prospectus gives a **floor price**. The issue price is **never below face value**. [SM 258]
- **Differential pricing** (SM short-essay question): retail investors and reserved employees may get a lower price, but **not lower than 10%** below the net-offer price. **Anchor investors** never pay less than other applicants. Under **alternate book building**, employees may pay up to **10%** below the floor price. [SM 259]
- **Face value:** it can be below ₹10 but not below **₹1**, and only if the issue price is **₹500** or more. If the issue price is below ₹500, the face value is **₹10**. [SM 259]

### 4.1.5 Promoters' contribution and lock-in [SM 259]

**CONTRIBUTION**
IPO: promoters bring **at least 20% of the post-issue capital** [SM 259]

→

**LOCK-IN: MINIMUM 20%**
**3 years** from the date of commercial production or the date of allotment, **whichever is later** [SM 259]

→

**LOCK-IN: EXCESS OVER 20%**
**1 year**. In a further public offer, the excess is **not** locked in [SM 259]

**⚠ CHECK AMENDMENT**
In 2021 SEBI shortened these lock-ins (to 18 months and 6 months) for issues whose money is not for capital expenditure. The SM still says 3 years and 1 year, and its own True/False answer key says "locked in for 3 years" is True. **Write the SM figures**, and add the 2021 change in one line if you like.

### 4.1.6 Book building: who gets how much [SM 259–260]

**SM WORDS** "Book Building means a process undertaken to elicit demand and to assess the price for determination of the quantum or value of specified securities." *(This is Jun'26 Q1(x).)* [SM 259]

| Category in the net offer to public | Book building: normal | Book building: QIB route (Reg 6(2)) | Not book built (fixed price) |
|---|---|---|---|
| Retail individual investors | not less than **35%** | not more than **10%** | minimum **30%** |
| Non-institutional investors | not less than **15%** | not more than **15%** | the rest: other individuals, corporates, institutions |
| Qualified institutional buyers | not more than **50%** (5% of it for mutual funds) | not less than **75%** (5% of it for mutual funds) | |

Book building: up to **60%** of the QIB portion may go to **anchor investors**. Mutual funds also compete for the rest of the QIB portion. Fixed price: an unsubscribed part of one category can go to the other. If retail investors are entitled to more than **50%** on a proportionate basis, they get that higher share. [SM 259–260]

**DEC'26 SUPPLEMENTARY: SEBI (ICDR) (AMENDMENT) REGULATIONS, 2026 · NOTIFIED AND EFFECTIVE 21 MARCH 2026**

- **Draft Abridged Prospectus:** a public issuer must prepare and file it with the **draft offer document**. The draft and final abridged prospectus are made available with their offer documents. [Supp Dec'26 p.6]
- **Pledged pre-issue securities stay locked in:** the lock-in still applies when they are pledged. [Supp Dec'26 p.6]

**EXAM ANGLE: 4.1**

- **Asked as long questions:** Dec'23 Q7(a) 7m, "cannot make a public issue… explain the conditions" (SM 4.1.1 (a)–(j)). Dec'25 Q7(a) 7m, "IPO eligibility: net worth, net tangible assets, operating profit… and why" (4.1.3, both routes, plus the "why" lines). ICMAI postal Q4(b) 6m, "requirements for a first public issue".
- **Asked as MCQs:** promoters' minimum contribution 20% (Dec'23) · minimum subscription 90% (Jun'24) · book building (Jun'26) · SEBI's three functions (Dec'24, Jun'25) · ICMAI MQP: net tangible assets ₹3 crore.
- **Answer frame, 7 marks:** one opening line naming the SEBI (ICDR) Regulations, 2018 → the conditions as numbered points in SM order, numbers in bold → for "why", two lines → one closing line.

## 4.2 Insider Trading (SEBI PIT Regulations, 2015)

**WHAT IT IS** Insider trading means trading in a listed company's securities, or passing on information, while holding **unpublished price sensitive information (UPSI)** that the market does not have. The SEBI (Prohibition of Insider Trading) Regulations, 2015 ban it and make every listed company keep codes, controls and disclosures in place. [SM 261]

### 4.2.1 Definitions: the case questions turn on these [SM 261–262]

| Term | Meaning |
|---|---|
| **Insider** | SM WORDS any person who is (i) a **connected person**; or (ii) **in possession of or having access to** unpublished price sensitive information. [SM 262] |
| **Connected person** | anyone who **is, or during the 6 months before** the act was, associated with the company in any capacity, in a way that gives or can reasonably be expected to give access to UPSI. Examples: frequent communication with its officers; a contractual, fiduciary or employment relationship; director, officer or employee; a professional or business relationship. [SM 261] |
| **Deemed connected** (unless the contrary is shown) | immediate relatives of the above · holding, associate or subsidiary company · intermediaries under s.12 of the SEBI Act, with their employees and directors · investment company, trustee company or AMC, with their employees and directors · officials of a stock exchange or clearing house · MF trustees and AMC directors or employees · directors or employees of a public financial institution · officials of a SEBI-recognised self-regulatory organisation · the company's **banker** [SM 261] |
| **Immediate relative** | the **spouse**, plus the **parent, sibling and child** of the person or of the spouse, if they are **financially dependent** on the person or **consult** the person on trading decisions. [SM 261–262] |
| **UPSI** | SM WORDS information relating to a company or its securities, directly or indirectly, that is **not generally available**, which upon becoming generally available is **likely to materially affect the price**. Ordinarily it includes: **(i) financial results (ii) dividends (iii) change in capital structure (iv) mergers, de-mergers, acquisitions, delistings, disposals and expansion of business (v) changes in key managerial personnel**. [SM 262] |
| **Generally available information** | information **accessible to the public on a non-discriminatory basis**. [SM 261] |
| **Compliance officer** | a senior officer, **financially literate**, who reports to the board. Responsible for policies, procedures, records, preserving UPSI, monitoring trades and implementing the codes, under the board's overall supervision. [SM 261] |

**MEMORY HOOK: THE 5 KINDS OF UPSI**

**R-D-C-M-K:** Results, Dividends, Capital structure, Mergers (and the rest of M&A), KMP changes.

### 4.2.2 The two bans: communicating and trading [SM 262]

**BAN 1: NO COMMUNICATING UPSI**

- No insider shall communicate, provide or allow access to UPSI about a listed (or to-be-listed) company, **except for legitimate purposes**. The board writes a **"legitimate purposes" policy** as part of the Codes of Fair Disclosure and Conduct. [SM 262]
- Insiders are given **due notice** to keep UPSI confidential. [SM 262]
- **Allowed for a transaction** that (a) requires an **open offer**, or (b) the board decides is in the **company's best interests**, provided the UPSI is made generally available at least **2 trading days** before the transaction. The receiving parties sign confidentiality and non-disclosure agreements and must not trade while they hold UPSI. [SM 262]
- **Structured digital database (SDD)** of the UPSI shared, with internal controls, kept for at least **8 years** (longer if there is an investigation). [SM 262]

**BAN 2: NO TRADING WHILE HOLDING UPSI**

- No insider shall trade in securities listed or proposed to be listed **when in possession of UPSI**. The insider may prove innocence through the defences in the Regulations (the SM does not list them). [SM 262]
- **Onus:** a **connected person** must prove they did **not** have UPSI. For anyone else, the onus is on **SEBI** (the SM says "the Board"). [SM 262]

*Jun'26 MCQ (xi): the correct option said UPSI may be shared only for "legitimate purposes, performance of duties, or legal obligations". That is the Regulation's full wording; the SM shortens it to "legitimate purposes".*

### 4.2.3 Trading plan [SM 263]

**1 · INSIDER** draws up a trading plan [SM 263] → **2 · COMPLIANCE OFFICER** approves it [SM 263] → **3 · PUBLIC DISCLOSURE** the compliance officer notifies the stock exchanges [SM 263] → **4 · WAIT** trading starts **no earlier than 6 months** after public disclosure [SM 263] → **5 · TRADE** exactly as planned; **no deviation** [SM 263]

### 4.2.4 Disclosures of trading [SM 263]

- These cover trades by the insider, their **immediate relatives**, and anyone for whom the insider takes trading decisions. [SM 263]
- **Initial:** a KMP or director discloses their holding **as on the date of appointment**. · **Continual:** within **2 trading days** of a trade, if the value traded in a **calendar quarter** exceeds **₹10 lakh**. [SM 263]

#### 4.2.5 CODE OF FAIR DISCLOSURE (Schedule A): the board writes it, publishes it on the website and sends it to the stock exchanges

1. **Prompt public disclosure** of UPSI as soon as credible, concrete information exists; uniform dissemination, so that no one gets a **selective disclosure**
2. A **chief investor relations officer** (a senior officer) handles dissemination
3. A fair response to **queries on news reports** and to regulators' requests to verify **market rumours**
4. Nothing shared with **analysts or research staff** is UPSI
5. **Transcripts or records** of analyst meetings are put on the official website

[SM 263]

#### 4.2.6 CODE OF CONDUCT (Schedule B): drawn up by the CEO or MD, for designated persons and their immediate relatives

- The board, with the compliance officer, names the **designated persons** by their role and access to UPSI [SM 263–264]
- The compliance officer reports to the board and the **Audit Committee** [SM 264]
- The **trading window** reopens **not earlier than 48 hours** after the UPSI becomes generally available [SM 264]
- While the window is open, trades above the board's threshold need **pre-clearance**. The compliance officer may ask for a declaration of "no UPSI" [SM 264]
- A pre-cleared trade must be done within **7 trading days**, or a fresh pre-clearance is needed [SM 264]
- Formats, sanctions and disciplinary action are set out. Designated persons give **names and PAN** of specified persons every year and whenever these change [SM 264]

### 4.2.7 Institutional mechanism to prevent insider trading [SM 264]

| # | Who | Duty |
|---|---|---|
| 1 | **CEO** | puts in place **adequate and effective internal controls** for compliance [SM 264] |
| 2 | **Audit Committee** | reviews compliance **at least once in a financial year** and checks that the internal controls are adequate and working [SM 264] |
| 3 | **Listed company / board** | a board-approved **policy for inquiry into a leak or suspected leak** of UPSI; inquires on time and informs **SEBI** promptly [SM 264] |
| 4 | **Listed company** | a **whistle-blower policy**, made known to employees so they can report leaks [SM 264] |
| 5 | **Intermediaries & fiduciaries** | **co-operate** with the company's inquiry into a leak [SM 264] |

**EXAM ANGLE: 4.2 (4 LONG QUESTIONS IN 7 PAPERS)**

- **Jun'23 Q5(a) 8m** "steps by a listed company to prevent insider trading": the 5-point mechanism + code of conduct (trading window, pre-clearance, 7 days) + code of fair disclosure + the structured digital database. **Dec'24 Q6(a) 7m** "describe insider trading + institutional mechanism": definitions, the two bans, then the 5 points. **Jun'26 Q7(a) 7m** "prohibition on communicating UPSI and trading": 4.2.2 in full.
- **Jun'24 Q5(a) 7m, case:** Ranjan, CMD of GIPL, sold GIPL shares before the termination of two shareholders' agreements was told to the NSE. His plea: the sale was part of a corporate restructuring to save the parent company, and that was found true. Asked: (1) Is he an insider? (2) What is UPSI? (3) Is SEBI's charge correct?
  **Frame:** provision (insider, connected person, UPSI, trading ban, onus) → facts (as CMD he is a **connected person, so an insider**; the termination was not yet public and was price-sensitive, so it was **UPSI**) → conclusion. On (3): these facts match the Supreme Court's decision in **SEBI v. Abhijit Rajan (2022)**. There the court held that a sale **forced by a genuine restructuring**, not driven by the UPSI, is not insider trading, so SEBI's charge failed. **⚠ This case is not in the SM. Check it against ICMAI's suggested answer once Hima downloads it.**

## 4.3 Takeover Code (SEBI SAST Regulations, 2011)

**WHAT IT IS** When someone (the **acquirer**) buys enough shares, voting rights or control of a listed company (the **target**), the takeover code makes them disclose it and **offer the other shareholders an exit** at a fair price (the **open offer**). It covers direct and indirect acquisitions. It does **not** apply to a company listed without a public issue on the **Innovators Growth Platform**. [SM 265]

### Key definitions [SM 265–266]

| Term | Meaning (short) |
|---|---|
| **Acquirer** | anyone who acquires, or agrees to acquire, shares, voting rights or control in a target, directly or indirectly, alone or through **persons acting in concert** [SM 265] |
| **Control** | the right to **appoint a majority of the directors** or to **control management or policy decisions**, through shareholding, management rights, shareholders' or voting agreements, or any other way [SM 265] |
| **Persons acting in concert (PAC)** | persons with a **common objective** of acquiring shares, voting rights or control, who co-operate under a formal or informal agreement. **Deemed PACs:** a company + its holding, subsidiary and same-management companies · a company + its directors + its managers · promoters + promoter group · immediate relatives · a mutual fund + its sponsor, trustees and AMC · a CIS + its management company · a VCF or AIF + its sponsor, trustees and manager · a merchant banker or portfolio manager + a client who is an acquirer [SM 265–266] |
| **Target company** | a company or body corporate set up under Central, State or Provincial law, **whose shares are listed** on a stock exchange [SM 266] |
| **Frequently traded shares** | turnover in the **12 calendar months** before the month of the public announcement is at least **10%** of the total shares of that class [SM 265] |
| **Offer period / tendering period** | offer period: from the agreement to acquire (or the public announcement) until payment or withdrawal · tendering period: the window, **10 working days**, in which shareholders tender their shares [SM 265–266] |
| **VWAMP / VWAP** | volume-weighted average **market** price (all trades on the exchange) / volume-weighted average price (shares the acquirer **bought**) [SM 266] |

**⚠ "IDENTIFIED DATE": THE SM AND THE REGULATION DIFFER**

SM: "10 working days after closure of the offer". Regulation: the **10th working day before the tendering period starts** (it decides who gets the letter of offer). An MCQ asks the number, which is 10 either way; in a written answer use the Regulation's meaning. [SM 265]

#### 4.3.1 KINDS OF TAKEOVER (Jun'26 MCQ, PTP Q7(a))

| | |
|---|---|
| **Friendly** | promoters **sell voluntarily** at an attractive price |
| **Hostile** | promoters **resist** and defend control |
| **Horizontal** | a company in the **same industry** |
| **Vertical** | a **supplier or customer** (backward or forward integration) |
| **Conglomerate** | a company in a **totally different industry** |

Hook: by attitude (Friendly / Hostile); by business link (Horizontal / Vertical / Conglomerate). [SM 266]

#### DISCLOSURES (PTP Q7(a))

- **Event-based:** the duty is on the **acquirer, promoters and PACs**, never the target. Acquisitions include taking shares as an encumbrance; disposals include releasing them (not for scheduled commercial banks or PFIs taking a pledge). [SM 266]
- **Continual (Reg 30):** holding as on **31 March**, filed within **7 working days** of the year-end with every stock exchange and the target's registered office. Filed by **promoters** (whatever they hold) and **non-promoters holding more than 25%** with their PACs. [SM 266–267]
- **Encumbrance (Reg 31):** a promoter discloses the creation, invocation or release of a pledge, lien or similar within **7 working days**, to the stock exchanges and the target. [SM 267]

## 4.3.2 When is an open offer compulsory? [SM 267]

**BELOW 25%**
may buy; event-based disclosures only

→

**CROSSES 25%**
the acquirer with PACs reaches or exceeds **25%** of voting rights → public announcement of an open offer for at least **26%** more [SM 267]

→

**ALREADY 25% OR MORE (Reg 3(2))**
more than **5%** in any financial year (from 1 April) → open offer for **26%** [SM 267]

→

**CEILING**
never above the **maximum permissible non-public shareholding**; the **25%** minimum public float stays [SM 267]

### 4.3.3 VOLUNTARY OPEN OFFER: PRE-CONDITIONS

a. already holds at least **25%**
b. no acquisition in the preceding **52 weeks** without an open offer (no creeping acquisition)
c. no buying during the offer period except under the offer
d. no buying for **6 months** after the offer, except by another voluntary or competing offer
e. may be made conditional on a minimum level of acceptance

[SM 267]

### 4.3.4 WITHDRAWAL OF OFFER (Reg 23): ONLY IF

i. statutory approvals are **refused**
ii. the acquirer, a natural person, has **died**
iii. a condition in the acquisition agreement is not met
iv. SEBI thinks the circumstances merit withdrawal

The manager to the offer announces it in the newspapers within **2 working days**, with reasons, and informs SEBI, the stock exchanges and the target. [SM 267–268]

## 4.3.5 The open-offer timeline [SM 268–269]

**ESCROW**
opened at least **2 working days** before the detailed public statement [SM 268]

→

**DRAFT LETTER TO SEBI**
within **5 working days** of the detailed public statement, with the fee; copy to the target and the exchanges [SM 268]

→

**SEBI COMMENTS**
or **15 working days** pass with none [SM 268]

→

**LETTER OF OFFER DISPATCHED**
within **7 working days** of the comments (or of the 15-day expiry) [SM 268]

**IDs' RECOMMENDATION (4.3.8)**
published at least **2 working days** before tendering, same newspapers; copy to SEBI, exchanges, manager [SM 269]

→

**TENDERING PERIOD**
starts within **12 working days** of SEBI's comments; open for **10 working days** [SM 268]

→

**PAYMENT**
completed within **10 working days** of the last tendering day [SM 268]

→

**ESCROW RELEASED**
not before **30 days** after payment is completed [SM 268]

Also: the offer price may be revised up to **3 days** before the offer opens (SM). [SM 265] · **Escrow forms:** cash with a scheduled commercial bank; a bank guarantee in favour of the manager to the offer; frequently traded, freely transferable shares or other securities, with a margin. [SM 268] · **Payment by:** cash; listed shares of the acquirer or its PAC; listed secured debt rated at least investment grade; convertible debt convertible into the acquirer's listed shares. [SM 268]

### 4.3.7 OBLIGATIONS OF THE TARGET COMPANY (MQP Q7(a), Jun'25 Q4(b))

i. during the offer period the board runs the business **in the ordinary course**, as in the past
ii. **no record date** for a corporate action from the **3rd working day** before tendering starts until tendering ends
iii. gives the acquirer the **list of shareholders** (names, addresses, holdings, folio numbers, pending transfers) within **2 working days** of the identified date
iv. during the offer period, without a **special resolution by postal ballot**, the board of the target or its subsidiaries shall not **alienate material assets** (by sale, lease, encumbrance) outside the ordinary course

[SM 268–269]

### 4.3.9 OBLIGATIONS OF THE ACQUIRER (MQP Q7(a))

a. **firm financial arrangements** are in place for the payment
b. is able to implement the offer, subject to statutory approvals
c. **no alienation of the target's material assets** outside the ordinary course, unless the intention was declared in the detailed public statement and the letter of offer. If not declared: a special resolution by postal ballot, with reasons
d. the acquirer and PACs **shall not sell** target shares during the offer period
e. the acquirer and PACs are **jointly and severally responsible**

[SM 269]

**4.3.10 Exemptions** [SM 269]: ordinary-course acquisitions by a SEBI-registered **underwriter**, a **stock broker** exercising a lien for a client, or a **merchant banker / nominated investor in market making** · a **safety-net scheme** · a merchant banker acting as a **stabilising agent** · a **disinvestment** agreement · acquisitions under court-ordered **reconstruction, merger, amalgamation or demerger** · under the **SARFAESI Act, 2002** · under the **Delisting** regulations · on **forfeiture** of shares.

**DEC'26 SUPPLEMENTARY: SEBI (SAST) (AMENDMENT) REGULATIONS, 2025 · NOTIFIED 3 DEC 2025, EFFECTIVE 2 JAN 2026**

- If the target's shares are **not frequently traded**, the offer price is based on the valuation parameters adopted by an **independent registered valuer**. [Supp Dec'26 p.5]
- If the prescribed parameters cannot fix the offer price, the **fair price** is set by an independent registered valuer. SEBI may also require such a valuation, with the **cost borne by the acquirer**. [Supp Dec'26 p.5]

**EXAM ANGLE: 4.3**

- **Jun'25 Q4(b) 7m:** obligations of the target + exemptions · **ICMAI MQP Q7(a):** obligations of the target + acquirer (ICMAI's answer = SM 4.3.7 + 4.3.9 copied) · **PTP Q7(a):** kinds + disclosures · **MCQs:** escrow (Jun'24), conglomerate (Jun'26).
- **Dec'26, prepare:** "Explain the kinds of takeover and the obligations of the target company and the acquirer. How is the open-offer price fixed when shares are not frequently traded?" (last part: the amendment above). Model answer below.

**MODEL ANSWER: OUR TOP DEC'26 SEBI QUESTION (7 MARKS) · AS YOU WOULD WRITE IT IN THE ANSWER BOOK**

**Q.** Explain the kinds of takeover and the obligations of the target company and the acquirer under the SEBI (SAST) Regulations, 2011. How is the open-offer price fixed when the shares are not frequently traded?

**Introduction.** The SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (the Takeover Code) apply to the direct and indirect acquisition of shares or voting rights in, or control over, a listed target company. [SM 265]

**1. Kinds of takeover** [SM 266]

i. **Friendly takeover:** the promoters of the target voluntarily sell their shares to the acquirer at an attractive price.
ii. **Hostile takeover:** the promoters do not want to give up control and fight back.
iii. **Horizontal takeover:** of a company in the same industry.
iv. **Vertical takeover:** of a supplier or customer (backward or forward integration).
v. **Conglomerate takeover:** of a company in a totally different industry.

**2. Obligations of the target company** [SM 268–269]

i. During the offer period the board shall conduct the business in the **ordinary course**, consistent with past practice.
ii. No **record date** for a corporate action on or after the **third working day** before the tendering period starts, until it ends.
iii. Give the acquirer, within **two working days** from the identified date, the **list of shareholders** and of pending transfer applications.
iv. Without a **special resolution by postal ballot**, the board of the target or its subsidiaries shall not **alienate material assets** outside the ordinary course during the offer period.
v. The **independent directors' recommendation** is published at least two working days before the tendering period starts.

**3. Obligations of the acquirer** [SM 269]

a. Ensure **firm financial arrangements** for the payment obligations.
b. Ensure it is able to **implement the open offer**, subject to statutory approvals.
c. Not **alienate material assets** of the target unless the intention was declared in the detailed public statement and the letter of offer; otherwise a special resolution by postal ballot is needed.
d. The acquirer and PACs shall **not sell** target shares during the offer period.
e. The acquirer and PACs are **jointly and severally responsible** for the obligations.

**4. Offer price when shares are not frequently traded.** Under the SAST (Amendment) Regulations, 2025 (effective 2 January 2026), the price is based on the valuation parameters adopted by an **independent registered valuer**. Where the prescribed parameters cannot fix it, the fair price is set by an independent registered valuer, and SEBI may require such a valuation at the **acquirer's cost**. [Supp Dec'26 p.5]

**Conclusion.** The Code lets control change hands while protecting public shareholders: business as usual during the offer, assets kept intact, and a fair exit price.

Built from the SM text. ICMAI's own MQP answer to the obligations part copies the same SM lists. Spend about 12 minutes; write headings and numbered points, not paragraphs.

# M4 Mind map: the whole module on one page

### 4.1 IPO: who cannot issue (ICDR 2018)

- **People:** debarred by SEBI · wilful defaulter
- **Paperwork:** no in-principle listing application · no depository agreement · partly paid shares · promoters not in demat
- **Money:** firm finance < 75% · GCP > 25% · open 3–10 days · minimum subscription 90% (refund in 15 days)
- **Appoint:** lead merchant banker · syndicate or bankers · Registrar · compliance officer

### 4.1 IPO: entry tests and money

- **Route 1** (all 4): NTA ₹3 cr ×3 yrs (≤50% monetary) · op. profit ₹15 cr (best 3 of 5) · net worth ₹1 cr ×3 · name change → 50% revenue
- **Route 2:** book building, ≥75% to QIBs, else refund
- 1,000 allottees · >₹100 cr → monitoring to 95%
- Promoters 20%; lock-in 3 yrs / 1 yr ⚠
- Book building 35/15/50 · QIB route 10/15/75 · anchor 60% · fixed price retail 30%

### 4.2 Insider (PIT 2015): who and what

- **Insider** = connected person OR in possession of / access to UPSI
- **Connected** = associated in the last 6 months, with access to UPSI; deemed list: relatives, group companies, intermediaries, AMCs, exchange officials, banker…
- **Immediate relative** = spouse + parent, sibling, child (dependent or consulted)
- **UPSI** = not generally available + price-sensitive: R-D-C-M-K

**SEBI**
Module 4 · SM 255–272

protect · develop · regulate
quasi-legislative · quasi-judicial · quasi-executive

ICDR 2018 · PIT 2015 · SAST 2011

### 4.2 Insider: rules

- **Ban 1:** no communicating, except for legitimate purposes · open offer, or board + public 2 trading days before · SDD 8 yrs
- **Ban 2:** no trading with UPSI · onus on the connected person
- Trading plan: 6-month gap, no deviation · disclosure: 2 trading days if > ₹10 lakh a quarter
- Codes: fair disclosure (Sch A) · conduct (Sch B): window 48 h, pre-clearance, 7 trading days
- **Mechanism:** CEO controls · Audit Committee yearly · leak inquiry · whistle-blower · intermediaries co-operate

### 4.3 Takeover (SAST 2011): triggers

- **Kinds:** Friendly / Hostile · Horizontal / Vertical / Conglomerate
- **Open offer:** crossing 25% → offer for 26% · already ≥ 25%: > 5% a year → offer · keep 25% public float
- **Disclosures:** event-based (acquirer, not the target) · Reg 30, 31 March, 7 WD · Reg 31 encumbrance, 7 WD
- **Voluntary offer:** holds 25% · none in 52 weeks before · none for 6 months after
- **Withdrawal (Reg 23):** approvals refused / death / condition not met / SEBI

### 4.3 Takeover: process and duties

- **Timeline:** escrow 2 WD before the public statement → draft letter of offer 5 WD → SEBI 15 WD → dispatch 7 WD → tendering starts within 12 WD, lasts 10 WD → payment 10 WD → escrow released after 30 days
- **Target:** ordinary course · no record date from the 3rd WD before tendering · shareholder list in 2 WD · no alienation without a special resolution by postal ballot · IDs recommend 2 WD before tendering
- **Acquirer:** firm finance · able to implement · no alienation · no selling · jointly and severally liable
- **Dec'26:** independent registered valuer for shares not frequently traded

## R Revision sheet: every number in the module

| 4.1 IPO | Number |
|---|---|
| firm finance arranged (of the means of finance) | 75% |
| general corporate purposes, maximum | 25% |
| issue open: minimum – maximum | 3 – 10 days |
| minimum subscription / refund within | 90% / 15 days |
| net tangible assets, each of 3 years (monetary assets at most 50%) | ₹3 crore |
| average operating profit (best 3 of 5 years) | ₹15 crore |
| net worth, each of 3 years | ₹1 crore |
| name change: revenue from the new activity | 50%, last 1 year |
| convertible-debt IPO: no default for | 6 months |
| minimum prospective allottees | 1,000 |
| monitoring if the issue is above … until … used | ₹100 cr / 95% |
| retail / employee price discount, maximum | 10% |
| face value below ₹10 (minimum ₹1) only if the price is at least | ₹500 |
| promoters' minimum contribution (post-issue) | 20% |
| lock-in: minimum contribution / excess ⚠ | 3 yrs / 1 yr |
| book building: retail / NII / QIB | ≥35 / ≥15 / ≤50% |
| QIB route: retail / NII / QIB | ≤10 / ≤15 / ≥75% |
| mutual funds (within QIB) / anchor (of QIB) | 5% / 60% |
| fixed price: retail minimum | 30% |
| **4.2 Insider trading** | **Number** |
| connected person: look-back | 6 months |
| UPSI made public before the transaction | 2 trading days |
| structured digital database kept | ≥ 8 years |
| trading plan: earliest trade after disclosure | 6 months |
| continual disclosure: within / if more than | 2 trading days / ₹10 lakh a quarter |
| trading window reopens, not earlier than | 48 hours |
| pre-cleared trade executed within | 7 trading days |
| Audit Committee review | once a financial year |

| 4.3 Takeover | Number |
|---|---|
| initial trigger → offer size | 25% → 26% |
| creeping limit a year (already ≥ 25%) | 5% |
| minimum public float | 25% |
| frequently traded: turnover in 12 months | ≥ 10% |
| Reg 30 / Reg 31 disclosures within | 7 working days |
| non-promoter continual disclosure if holding more than | 25% |
| voluntary offer: no buying before / after | 52 weeks / 6 months |
| withdrawal announced within | 2 WD |
| escrow before the detailed public statement | 2 WD |
| draft letter of offer / SEBI comments / dispatch | 5 / 15 / 7 WD |
| tendering starts within / lasts | 12 / 10 WD |
| payment after tendering / escrow release | 10 WD / 30 days |
| IDs' recommendation before tendering | 2 WD |
| no record date from … before tendering | 3rd WD |
| shareholder list to the acquirer | 2 WD |
| offer price revision, up to (SM) | 3 days before |
| identified date ⚠ | 10 WD |
| **Related (Module 3, Dec'26 supplementary)** | **Number** |
| HVDLE threshold, raised from ₹1,000 cr | ₹5,000 crore |

WD = working days. ⚠ = see the note in the topic. Sources: SM 257–269, Dec'26 supplementary pp. 5–6.

## Q The SM's own exercise: the exam has copied it 5 times

### MCQs [SM 270–272]

| # | Question (short) | Answer |
|---|---|---|
| 1 | maximum days an issue is kept open | **10** |
| 2 | at IPO the issuer must have a | **designated compliance officer** ⚠ |
| 3 | which does not need a prospectus | **bonus issue** ⚠ |
| 4 | minimum face value can be | **₹1** |
| 5 | takeover means | **acquiring shares giving control over management** |
| 6 | SEBI's Preamble: to protect / develop / regulate | **all of the above** |
| 7 | not a function of SEBI *(Dec'24, Jun'25)* | **quasi-official** |
| 8 | banking company director: prior approval of | **RBI** |

⚠ The SM's printed key gives "b" for Q2 and "c" for Q3, which looks swapped. ICMAI's MCQ bank (Q144, Q145) gives the answers shown here.

### True / False

| | |
|---|---|
| SEBI regulations normally apply to public issues | **T** |
| promoters' contribution locked in for 3 years | **T** |
| only a company secretary can be the compliance officer | **F** |
| change in capital structure is UPSI | **T** |
| SEBI (SAST) regulations and the takeover code are the same | **T** |

### Fill in the blanks

| | |
|---|---|
| minimum promoters' contribution in an IPO *(Dec'23)* | **20%** |
| promoters transfer voluntarily: … takeover | **friendly** |
| open-offer money is kept in an … account *(Jun'24)* | **escrow** |
| identified date: … working days | **10** |
| minimum subscription, % of issue size *(Jun'24)* | **90** |

### ICMAI MCQ bank, SEBI items (Q143–149 = the SM exercise)

| | |
|---|---|
| pre-cleared trades must be executed within (Q267) | **7 trading days** |
| hostile takeover is (Q268) | **without the promoters' consent** |
| connected person: onus of proving no UPSI is on (Q269) | **the connected person** |
| minimum public float after acquisition (Q270) | **25%** |
| not an "encumbrance" (Q271) | **dividend declaration** |

### Essay questions in the SM: practise these

- Differential pricing (4.1.4) · lock-in period (4.1.5) · define UPSI (4.2.1)
- Book building process (4.1.6) · the three requirements for a first public issue (4.1.3) · "connected person" (4.2.1)

# Module 5 · The Competition Act, 2002

P13 · Section B · topics 5.1–5.2

SM pp. 273–294 (22 pages). **56 marks in 7 papers. A Competition long question in every paper** (Q7(b) or Q8(a), swapping with FEMA), plus an MCQ in the (x)–(xii) block almost every time. Section numbers the SM does not print are taken from the Act.

| Paper | What was asked | Marks |
|---|---|---|
| Jun'23 | MCQ: appeal to the SC within **60 days** (= SM MCQ 11) · Q5(b) **abuse of dominance** and **predatory pricing** | 2 + 8 |
| Dec'23 | MCQ: abuse of dominance does not include a price-fixing agreement · Q7(b) **penalty for offences in furnishing information** (s.45) | 2 + 7 |
| Jun'24 | MCQ: deemed approval of a combination · Q6(b) **division of a dominant enterprise** (s.28) | 2 + 4 |
| Dec'24 | MCQ: combination turnover threshold (= SM MCQ 2) · Q6(b)(i) **abuse of dominant position** | 2 + 4 |
| Jun'25 | MCQ: unfair competition (= SM MCQ 8) · Q6(b) **s.45 penalty again** | 2 + 7 |
| Dec'25 | MCQ: a buyer for resale is a "consumer" · Q7(b) **car maker controls dealer discounts** (resale price maintenance) | 2 + 7 |
| Jun'26 | Q8(a) **objectives and key provisions; role of the CCI** on agreements and dominance | 7 |

**HOW IT IS EXAMINED · DEC'26 PREDICTION**

- **MCQs are SM exercise MCQs** (2, 8, 11; predatory pricing = MCQ 4; cartel = MCQ 9 in the PTP).
- Long favourites: **abuse of dominance** (3×), **s.45 penalties** (2×). Our Dec'26 picks: (1) **dominance + the s.19(4) factors** (ICMAI MQP Q7(b)); (2) **combinations and CCI orders** (PTP Q7(b), never asked long); (3) the **Director General's** role (postal).
- MCQ (x)–(xii): a **90%** chance of a Competition fact.

**MAP**

1. Background, objectives, definitions ★★
2. Anti-competitive agreements (s.3) ★★★
3. Abuse of dominance (s.4) and its factors ★★★
4. Combinations (s.5, 6, 20, 29, 31) ★★
5. CCI: constitution, powers, orders, s.28 division ★★
6. Penalties (s.42–46), appeals ★★
7. Model answers · SM exercise · numbers

## 5.1 Background, objectives, definitions · Jun'26 Q8(a)

**BACKGROUND · OBJECTIVES**

- The **MRTP Act, 1969** (in force 1 June 1970) aimed at curbing monopolies. A committee in **October 1999** recommended a modern law to **promote competition**, leading to the **Competition Act, 2002**, enacted on **13 Jan 2003** and amended in 2007. The MRTP Act was repealed (SM MCQ 1). [SM 275]
- The **CCI** was set up on **14 Oct 2003**; the agreements and dominance provisions were notified on **20 May 2009**. [SM 275]
- **Objectives:** (i) **prevent anti-competitive practices**; (ii) **promote and sustain competition**; (iii) **protect consumers' interests**; (iv) **ensure freedom of trade**; (v) **competition advocacy**. [SM 275]

**KEY DEFINITIONS**

- **Agreement**: any arrangement, understanding or action in concert, formal or not, written or not, enforceable or not. [SM 275]
- **Cartel**: an association of producers, sellers, distributors, traders or service providers who by agreement **limit or control production, distribution, sale or price** (SM MCQ 9). [SM 275–276]
- **Consumer**: a buyer of goods or hirer of services for consideration (paid, promised or deferred), **whether for resale, commercial purpose or personal use**. *Dec'25 MCQ: a refrigerator trader who bought for resale and has not yet paid **is a consumer** (option B).* [SM 276]
- **Enterprise**: a person or Government department in production, supply, distribution, services, investment or securities, but **not sovereign functions** (atomic energy, currency, defence, space). [SM 276]
- **Relevant market** = relevant **product** market (interchangeable or substitutable products) and/or relevant **geographic** market (an area of distinctly homogeneous conditions). [SM 277]
- Also: acquisition · goods (incl. shares after allotment, imports) · person · price. [SM 275–277]

## s.3 Anti-competitive agreements · Dec'25 Q7(b)

**WHAT IT IS** Any agreement on production, supply, distribution, storage, acquisition or control of goods or services that **causes or is likely to cause an appreciable adverse effect on competition (AAEC)** in India is **void**. **Horizontal** agreements are between enterprises at the **same level** (competitors); **vertical** ones are between **different stages** of the production and distribution chain. [SM 277]

### HORIZONTAL (incl. cartels): PRESUMED TO HAVE AAEC

a. directly or indirectly **fixing purchase or sale prices**
b. **limiting or controlling** production, supply, markets, technical development or investment
c. **sharing markets** or sources of production by geography
d. **bid rigging or collusive bidding** (reducing or manipulating competition in bids)

Joint-venture efficiency agreements are excepted. *Unfair competition = collusive price fixing, market allocation, discriminatory pricing: all of them (SM MCQ 8 = Jun'25 MCQ).* [SM 277–278]

### VERTICAL: VOID IF THEY CAUSE AAEC

- **Tie-in arrangement**: buying one product is made a condition of buying another. [SM 278]
- **Exclusive supply**: the buyer cannot deal in others' goods (*SM example: Soni Brothers may not supply anyone but ABC*). [SM 278]
- **Exclusive distribution**: limiting supply, or allocating areas or markets. [SM 278]
- **Refusal to deal**: restricting to whom goods are sold or from whom bought. [SM 278]
- **Resale price maintenance**: the buyer must resell at prices the seller stipulates, unless lower prices are clearly allowed (hence the "MRP" printed on packs). [SM 278]

**Not covered:** (a) the right to restrain **infringement of IPRs** (copyright, patents, trade marks, GIs, designs, layout designs); (b) agreements relating **exclusively to exports**. **Leniency**: a cartel member who discloses honestly may get lenient treatment (s.46). [SM 277–278]

## s.4 Abuse of dominant position · Jun'23 Q5(b), Dec'24 Q6(b), ICMAI MQP Q7(b)

### DOMINANT POSITION · ABUSE

SM WORDS **"Dominant position"** means a position of strength, enjoyed by an enterprise, in the relevant market in India, which enables it to (i) **operate independently of competitive forces** in the relevant market; or (ii) **affect its competitors or consumers or the relevant market in its favour**. [SM 279]

**Abuse** (by an enterprise or group):

a. imposing **unfair or discriminatory conditions or prices**, including **predatory price**
b. **limiting production**, markets or technical development to consumers' prejudice
c. **denial of market access**
d. making contracts subject to **unconnected supplementary obligations**
e. **using dominance in one market to enter or protect another**

[SM 278–279]

SM WORDS **"Predatory price"** means the sale of goods or provision of services **at a price below cost** (as determined by regulations) of production, **with a view to reduce competition or eliminate competitors** (SM MCQ 4). [SM 279]
*Dec'23 MCQ: abuse does not include an **agreement to fix price**; that is s.3.*

### FACTORS FOR DOMINANCE (s.19(4)): THE MQP ANSWER

a. **market share**
b. **size and resources** of the enterprise
c. size and importance of **competitors**
d. **economic power**, including commercial advantage
e. **vertical integration**
f. **dependence of consumers**
g. monopoly or dominant position by statute or as a public sector company
h. **entry barriers**: regulatory, financial risk, high capital cost, marketing, technical, economies of scale, high cost of substitutes
i. **countervailing buying power**
j. **market size**
k. social obligations and costs
l. contribution to **economic development**
m. any other relevant factor

[SM 284]

### JUN'26 SUPPLEMENTARY: CCI (DETERMINATION OF COST OF PRODUCTION) REGULATIONS, 2025 (7 MAY 2025)

These replace the 2009 regulations for **predatory-pricing** cases under s.4. The main benchmark is **Average Variable Cost (AVC)** = total variable cost ÷ output (a proxy for marginal cost). Total cost, avoidable cost and LRAIC are also defined, and the CCI may use other measures (e.g. average total cost) with documented reasons. Expert advisers are formalised; the regulations apply prospectively. [Supp Jun'26 p.7]

## s.5–6 Combinations (mergers and acquisitions) · ICMAI PTP Q7(b)

**WHAT IT IS** A **combination** is an acquisition of an enterprise, acquisition of control, or a merger or amalgamation, where the parties **exceed the asset or turnover thresholds**. A combination that causes or is likely to cause an **AAEC in the relevant market in India is void**. [SM 279–280]

| Thresholds (SM) | In India | India + abroad |
|---|---|---|
| **Enterprises** (the parties) [SM 279] | assets **> ₹2,000 cr** or turnover **> ₹6,000 cr** | assets **> USD 1 bn** (incl. ₹1,000 cr in India) or turnover **> USD 3 bn** (incl. ₹3,000 cr in India) |
| **Group** [SM 279] | assets **> ₹8,000 cr** or turnover **> ₹24,000 cr** | assets **> USD 4 bn** (incl. ₹1,000 cr) or turnover **> USD 12 bn** (incl. ₹3,000 cr) |

Assets are at **book value** (less depreciation), as in the last audited accounts of the preceding year, **including brand, goodwill and IPRs**. The "group" exemption for those exercising less than **50%** of votes was continued for **5 years** (2016). The CG revises thresholds every **2 years** (WPI and exchange rates). [SM 279–280]

### NOTICE AND TIMELINE (SM)

- Notice to the CCI within **30 days** of (a) **Board approval** of the merger, or (b) **executing the agreement** for acquisition. [SM 280]
- No combination takes effect until **210 days** have passed or the CCI has passed orders, whichever is earlier. If there is no order in 210 days, it is **deemed approved** (SM MCQ 15; fill-in 3). [SM 280–282]
- **Exempt** from notice: share subscription, financing or acquisitions by a **PFI, FII, bank or VCF** under a loan or investment covenant, but details are filed within **7 days**. [SM 280]
- The CCI may inquire on its own within **1 year** after the combination takes effect. [SM 280]
- **Investigation:** show-cause, reply in **30 days** → DG's report → if prima facie AAEC, publication within **10 working days** of the CCI's direction (given within **7**), objections within **15 working days**, more information in **15** days → decision within **45 working days**. [SM 281]

### CCI ORDERS ON COMBINATIONS (s.31): THE PTP ANSWER

1. **no AAEC → approve**
2. **AAEC** → direct that it **shall not take effect**
3. AAEC that a **modification** can remove → **propose modification**. The parties carry it out in time (else deemed AAEC), or submit an **amendment within 30 working days**. If the CCI does not agree, a further **30 working days** to accept, else deemed AAEC
4. a void combination is dealt with by other authorities **as if it never happened**

**Factors (s.20(4)):** import competition · entry barriers · level of combination · countervailing power · likely price or margin increase · effective competition · substitutes · **market share** · removal of a vigorous competitor · vertical integration · **failing business** · innovation · economic development · whether **benefits outweigh harm**. CCI quorum **3**; casting vote with the chair. [SM 280–282]

### ⚠ THE SM'S MERGER-CONTROL FIGURES ARE PRE-2023 (NOT IN SM)

The **Competition (Amendment) Act, 2023** and the 2024 notifications: overall time limit **150 days** (not 210), with the CCI's prima facie view within **30 days**; a new **deal-value threshold** (transactions above ₹2,000 crore with substantial business in India); thresholds raised to **₹2,500 cr assets / ₹7,500 cr turnover** (parties) and **₹10,000 cr / ₹30,000 cr** (group). The SM's exercise answers (₹6,000 cr, 210 days) follow the SM. **For an MCQ, choose the SM figure if it is an option**; in a long answer, add the update in a line.

## 5.2 The Competition Commission of India: constitution, powers, orders · Jun'24 Q6(b), postal Q5(a)

### CONSTITUTION · DIRECTOR GENERAL

- A body corporate at **New Delhi**: a **Chairperson and 2 to 6 Members**, whole-time, appointed by the CG. Persons of ability, integrity and standing, with at least **15 years** in trade, economics, law, finance, accountancy, management, competition and similar fields. [SM 283]
- Term **5 years**, re-appointable (SM MCQ 12); retirement at **65**. [SM 283]
- The CG appoints a **Director General** to assist the CCI in **investigating contraventions**, plus a secretary, experts and officers (SM short essay: the DG's role). [SM 283]

### DUTIES AND POWERS (s.18, 19)

- Eliminate practices with adverse effect, promote and sustain competition, protect consumers, ensure freedom of trade. [SM 283]
- Inquire **on its own motion**, on **information from any person** or association, or on a **reference** from the CG, a State Government or a statutory authority. [SM 283]
- **AAEC factors (s.19(3)):** barriers to new entrants · driving out competitors · foreclosure · **benefits to consumers** · better production or distribution · technical, scientific and economic development. [SM 283–284]
- **Relevant geographic market:** trade barriers, local specifications, procurement policy, distribution, transport cost, language, preferences, after-sales needs. **Product market:** characteristics or end-use, price, preferences, in-house production, specialised producers, industrial classification. [SM 284–285]

### ORDERS AFTER INQUIRY (s.27)

a. **discontinue** the agreement or abuse and not re-enter it
b. **penalty**. **Cartels**: up to **3 times profit or 10% of turnover** for each year of continuance, **whichever is higher**
c. **modify** the agreement
d. abide by other orders, incl. **costs**
e. any other order; also against **other group members** responsible

[SM 285]

### DIVISION OF A DOMINANT ENTERPRISE (s.28) (Jun'24 Q6(b))

The CCI may, notwithstanding any other law, **order the division** of a dominant enterprise so that it does not abuse its dominance because of its size. The order may provide for: (a) **transfer or vesting** of property, rights, liabilities and obligations; (b) **adjustment of contracts**; (c) creation, allotment, surrender or **cancellation of shares** and securities; (d) **formation or winding up** of an enterprise; (e) **amendment of the MOA or AOA** (SM MCQ 14: all of these). [SM 285–286]

**Procedure (s.36):** natural justice; **civil court powers**; interim orders; experts; may direct production of documents to the DG. **Extra-territorial (s.32):** orders even if the agreement, the dominant enterprise or the combination is **outside India**, if it affects competition in India. [SM 286]

## s.42–46 Penalties, appeals, other · Dec'23 Q7(b), Jun'25 Q6(b)

| Default | Penalty |
|---|---|
| non-compliance with **CCI orders** (s.42) | up to **₹1 lakh a day**, maximum **₹10 crore**; if still not complied with or the fine not paid → **imprisonment** [SM 287] |
| failure to comply with directions of the **CCI (s.36) or DG (s.41)** (s.43) | up to **₹1 lakh a day**, maximum **₹1 crore** [SM 287] |
| party to a combination making a **false statement or omitting material facts** (s.44) | **₹50 lakh to ₹1 crore** [SM 287] |
| **s.45: offences in furnishing information**: (a) a statement or document known to be **false** in a material particular; (b) **omitting a material fact**; (c) **wilfully altering, suppressing or destroying** a document | fine up to **₹1 crore** [SM 287] |
| failure to give notice of a combination (s.43A) | up to **1%** of turnover or assets, whichever is higher (SM MCQ 13) |
| contravening **NCLAT** orders | up to **₹1 crore** or up to **3 years** in jail, or both [SM 289] |

**LESSER PENALTY (s.46): PART OF THE s.45 ANSWER**

- A **lesser penalty** is possible for a cartel member making a **full and true disclosure**. [SM 287]
- **Not** if the DG's investigation report (s.26) was received before the disclosure; **not** if the person stops **co-operating** until the proceedings end. [SM 287]
- **Withdrawn** if the conditions were breached, false evidence was given, or the disclosure was not vital; he may then be tried and penalised in full. [SM 287–288]
- **Companies (s.48):** the persons in charge are guilty too, unless they prove it was **without their knowledge** or they tried to prevent it; directors or officers who consented, connived or were negligent are liable. [SM 288]

**APPEALS · CG POWERS**

- **Appellate Tribunal = NCLAT** (since the COMPAT merged): hears appeals against CCI orders (s.26, 27, 28, 31, 32, 33, 38, 39, 43–46) and **compensation claims**. Appeal within **60 days** of receiving the order. [SM 288]
- The NCLAT has civil court powers but follows **natural justice**, not the CPC; its orders are executed as decrees. [SM 288–289]
- **Appeal to the Supreme Court within 60 days** (Jun'23 MCQ = SM MCQ 11). [SM 289]
- The CG may make rules, grant exemptions, give directions, and **supersede the CCI** for up to **6 months** in an emergency. The Act is **in addition to** other laws. [SM 289]

## 6 Model answers

**MODEL ANSWER 1 · CAR MAKER CONTROLS DEALER DISCOUNTS (DEC'25 Q7(b)) · 7 MARKS**

**Facts:** a car manufacturer set a customer-discount policy, told dealers not to discount beyond it, treated billing at old prices after a price rise as "unauthorised discounting", monitored this through agreements, and penalised dealers. Is it anti-competitive?

1. **Law:** s.3(1): an agreement causing an **AAEC** in India is void. s.3(4): **vertical** agreements between enterprises at different stages, including **resale price maintenance (RPM)**, are void if they cause an AAEC. RPM = selling goods on condition that the reseller charges the prices the seller stipulates, unless lower prices are clearly allowed. [SM 277–278]
2. **Applied:** the manufacturer and dealers are at **different stages**, so this is a vertical agreement. Capping discounts and penalising dealers who give more **fixes the minimum resale price**, which is RPM. It removes **intra-brand price competition** among dealers and harms consumers.
3. **AAEC factors (s.19(3)):** no **benefit to consumers**, who lose discounts; competition among dealers is **foreclosed**; no efficiency gain justifies it. [SM 283–284]
4. **Conclusion:** it is an anti-competitive vertical agreement (RPM) and **void**. The CCI may order the manufacturer to **cease and desist**, **modify** the agreements, and pay a **penalty** (s.27). [SM 285] (The CCI has penalised car makers on similar facts.)

**MODEL ANSWER 2 · DOMINANT POSITION AND ITS ABUSE (JUN'23 Q5(b), DEC'24 Q6(b), MQP Q7(b))**

(1) **Definition** of dominant position (s.4 Explanation), in the SM's words. (2) It is **not** an offence to be dominant; **abuse** is prohibited: list the five abuses (a)–(e). (3) **Predatory price** definition, and the 2025 cost regulations (AVC). (4) **Factors** the CCI considers (s.19(4)): market share, size and resources, competitors, economic power, vertical integration, consumer dependence, entry barriers, countervailing power, market size, and so on. (5) **Consequences**: s.27 orders (discontinue, penalty, modify) and **s.28 division** of the enterprise. [SM 278–286]

### The SM's own exercise for Competition (SM 290–294)

| | | | |
|---|---|---|---|
| 1 the Act replaced | **MRTP Act, 1969** | 8 unfair competition ★ | **all of the above** |
| 2 turnover threshold (enterprise, India) ★ | **₹6,000 crore** (SM) | 9 an association that limits production or price | **cartel** |
| 3 not an objective of the CCI | **promoting start-ups** ⚠ | 11 appeal to the SC within ★ | **60 days** |
| 4 selling below cost | **predatory pricing** | 12 term of members | **5 years** |
| 5 group asset limit abroad | **USD 4 billion** | 13 fine for no combination notice | **1%** |
| 6 not unfair competition | **tie-in purchase** (key) | 14 a division order may provide for | **all the above** |
| 7 not an objective of the Act | **to prevent competition** | 15 deemed approval after | **210 days** (SM) |

⚠ The SM's printed key for MCQ 3 says (c) "protect the interests of consumers", which IS an objective. The odd one out is (a) "promote start-ups". MCQ 10 in the SM exercise is a misplaced CSR question (key: mutual trust).

**True/False:** freedom of trade is an objective **T** · it replaced the Consumer Protection Act **F** · exclusive distribution presumed AAEC **T** (key) · combinations based on paid-up capital **F** (assets and turnover) · merge beyond the threshold just by intimating **F**. **Fill-ins:** regulated by the **CCI** · anti-competitive agreements presumed to have an **appreciable adverse effect** · deemed approval after **210** days · CCI at **New Delhi** · combinations are based on **turnover** (and assets).

## R Revision: numbers

| Rule | Number | Rule | Number |
|---|---|---|---|
| MRTP in force / Act enacted | 1 Jun 1970 / 13 Jan 2003 | CCI members / experience / term / age | 2–6 / 15 yrs / 5 yrs / 65 |
| CCI set up / s.3–4 notified | 14 Oct 2003 / 20 May 2009 | CCI quorum | 3 |
| enterprise: assets / turnover (SM) | ₹2,000 / ₹6,000 cr | cartel penalty | 3× profit or 10% turnover |
| global: USD 1 bn / USD 3 bn | incl. ₹1,000 / ₹3,000 cr | s.42: per day / max | ₹1 lakh / ₹10 cr |
| group: ₹8,000 / ₹24,000 cr | USD 4 / 12 bn | s.43: per day / max | ₹1 lakh / ₹1 cr |
| notice within / deemed approval (SM) | 30 / 210 days | s.44 / s.45 | ₹50 lakh–₹1 cr / ≤ ₹1 cr |
| FI covenant filing / CCI own inquiry within | 7 days / 1 year | NCLAT appeal / SC appeal | 60 / 60 days |
| modification: amend / accept | 30 + 30 working days | NCLAT order breach | ₹1 cr / 3 yrs |
| thresholds revised every | 2 years | CG supersedes CCI up to | 6 months |

# Module 6 · Foreign Exchange Management Act, 1999 P13 · Section B · topics 6.1–6.4

SM pp. 297–322 (26 pages). **60 marks in 7 papers.** FEMA swaps with Competition between **Q7(b) and Q8(a)**: one of them comes as a 7-marker almost every paper.

| Paper | What was asked | Marks |
|---|---|---|
| Jun'23 | Q6(a) notes: **prohibited sectors for FDI**; **parking of ECB proceeds** · Q8(b) **unlisted company issues 20% to a foreign investor**: possible? steps? (= SM solved case) | 8 + 6 |
| Dec'23 | Q8(a) **permitted investments by persons resident outside India** | 7 |
| Jun'24 | Q3(b) **restrictions on dealing in and holding foreign exchange** (s.3, s.4) | 7 |
| Dec'24 | Q7(a) **LRS**: eligible persons and purposes | 7 |
| Jun'25 | MCQ: an Indian company's shares issued to a Singapore resident = **Indian securities** · Q8(a) **late FC-GPR** filing case | 2 + 7 |
| Dec'25 | MCQ: ECB automatic route limit (**USD 750 million** = SM MCQ 7) · Q8(a) **returning resident's foreign assets**; capital vs current account | 2 + 7 |
| Jun'26 | Q7(b) **FDI framework**: routes, sectoral caps, reporting | 7 |

**HOW IT IS EXAMINED · DEC'26 PREDICTION**

- **SM headings become questions**: prohibited sectors (6.2.2), permitted investments (6.2.6), parking of ECB (6.3.3), LRS (6.4), s.3/s.4. Jun'23 Q8(b) is the SM's **solved case**.
- **Strongest Dec'26 FEMA pick: ECB**. It was revised by the **Dec'26 supplementary** (16 Feb 2026) and carried by 3 ICMAI practice papers (conversion of ECB into equity, parking, the limit). Also likely: **capital vs current account** + s.6(4) (Dec'25 repeat); FDI just asked (Jun'26).
- MCQ at (xiii)–(xv): an ECB, LRS or FDI fact; **insurance FDI 100%** and **land-border-country FDI → Government route** (supplementary).

**MAP**

1. FEMA basics, definitions, s.3–s.6 (6.1) ★★
2. FDI: meaning, prohibited sectors, routes, caps, pricing, reporting (6.2) ★★★
3. ECB and trade credits (6.3) ★★★
4. LRS (6.4) ★★
5. Supplementary changes ★★
6. Model answers · SM exercise · numbers

## 6.1 FEMA basics, definitions, and the core sections (s.3–s.6)

### FROM FERA TO FEMA

- Exchange control began under the Defence of India Act, **1939** → FERA **1947** → FERA **1973** (from 1 Jan 1974). After the **Tarapore Committee** (1997) on capital account convertibility, **FEMA 1999** came into force on **1 June 2000**. [SM 297]
- FEMA has **7 chapters, 49 sections**, with **5 sets of Rules** (CG, s.46) and **23 sets of Regulations** (RBI, s.47), RBI master directions, the DPIIT's FDI policy, and the **Enforcement Directorate**. [SM 297–298]
- It extends to **all of India** and to offices and branches abroad owned or controlled by residents. The **RBI** administers it in consultation with the CG. [SM 297–298]

### FERA vs FEMA

| FERA | FEMA |
|---|---|
| **regulate** and minimise dealings | **manage**; build a liberal forex market |
| everything specified is controlled | **everything not expressly covered is not controlled** |
| **criminal** law: arrest and imprisonment | **civil** law: penalties, not arrest |
| accused presumed guilty | the **ED must prove** guilt |
| – | **current account** transactions free unless restricted; **capital account** only as permitted |

[SM 298]

| Definition | Meaning |
|---|---|
| **Capital account transaction** s.2(e) | alters **assets or liabilities** (contingent included) **outside India of residents**, or **in India of non-residents** [SM 299] |
| **Current account transaction** s.2(j) | any transaction **other than** a capital account one: foreign trade and services payments, short-term banking credit, interest and net investment income, family maintenance abroad, travel, education, medical care [SM 299] |
| **Foreign exchange** s.2(n) | foreign currency, incl. deposits and balances in foreign currency; drafts, TCs, LCs, bills drawn in rupees but payable in foreign currency, or drawn abroad but payable in rupees [SM 299–300] |
| **Foreign security** s.2(o) | shares, bonds, debentures and other instruments **denominated in foreign currency**, even if returns are paid in rupees [SM 300] |
| **Person resident in India** s.2(v) | resident for **more than 182 days** in the preceding FY, except a person who left (or came) for employment, business or an uncertain stay. Also any person or body corporate registered in India, and offices or branches in or outside India controlled by residents (or non-residents) [SM 300–301] |
| Others | **Authorised person** (AD, money changer, offshore banking unit) · **FCCB** · **FDI** (in the DPIIT policy, not the Act) · **FII / FPI / FVCI** (SEBI-registered) · **PIO** (not Pakistan or Bangladesh) · repatriable investment [SM 298–300] |

### s.3 · s.4: RESTRICTIONS (Jun'24 Q3(b))

**s.3: no person shall** (i) deal in or transfer foreign exchange or foreign securities **except through an authorised person**; (ii) make any payment to or for a non-resident; (iii) receive a payment on a non-resident's behalf other than through an authorised person; (iv) enter into a financial transaction in India as consideration for acquiring an **asset outside India**. [SM 301]

**s.4: no resident shall** acquire, hold, own, possess or transfer foreign exchange, foreign securities or **immovable property outside India**, except as the Rules permit: property held by a **foreign citizen** resident in India; property acquired on or before **8 July 1947** with RBI permission; **gifts or inheritance** from them; property bought from an **RFC account**. [SM 301]

### s.5 · s.6: CURRENT AND CAPITAL ACCOUNT

**s.5 (current account):** free, except under the CAT Rules 2000: **Schedule I prohibited**, **Schedule II** needs Government/RBI approval, **Schedule III** has ceilings. [SM 301–302]

**s.6 (capital account):** through an authorised person, as RBI permits (classes and limits); no restriction on amortisation of loans or depreciation of direct investment. **s.6(4): a resident may keep, hold and invest foreign currency, securities or property acquired while he was resident outside India, or inherited from a non-resident** (the Dec'25 answer). Exporters must realise full export value; service exporters declare. [SM 302]

**Possession:** foreign **coins** without limit; currency within notified limits; a person not permanently resident may keep currency brought in and declared to customs without limit. **Foreign company's options:** a JV or WOS company, or a liaison, project or branch office. [SM 302–303]

## 6.2 Foreign Direct Investment (FDI) · Dec'23 Q8(a), Jun'23 Q6(a), Jun'26 Q7(b)

**WHAT IT IS** The FDI policy is set by the **DPIIT** (Ministry of Commerce and Industry) in a yearly **Consolidated FDI Policy**, under FEMA. The FEMA rules govern the mode, pricing and reporting. **FDI** = investment through capital instruments by a non-resident in an **unlisted** Indian company, or in **10% or more** of a **listed** company's post-issue paid-up equity (fully diluted). Below 10% in a listed company = **Foreign Portfolio Investment**; once FDI, it stays FDI even if it later falls below 10%. [SM 304]

### PROHIBITED SECTORS / PERSONS (Jun'23 Q6(a)(i))

1. **lottery** (Government, private, online)
2. **gambling and betting**, casinos
3. **chit funds** (except NRI/OCI on a non-repatriation basis)
4. **Nidhi** companies
5. trading in **TDRs**
6. **real estate business** and farm houses (not townships, residential or commercial construction, roads, bridges or REITs)
7. **cigars, cheroots, cigarillos, cigarettes** of tobacco or substitutes
8. sectors closed to private investment: **atomic energy**, **railway operations** (other than permitted)
9. citizens or entities of **Bangladesh or Pakistan**: only with **Government approval**; Pakistan never in defence, space or atomic energy

[SM 304–305]

### ROUTES · CAPS · INSTRUMENTS

- **Automatic route**: no prior approval of **RBI or Government** (SM MCQ 1). **Government route**: prior approval of the concerned ministry. [SM 305]
- **Sectoral caps**: up to **100% automatic** in sectors not listed in Regulation 16 of FEMA 20(R) and not prohibited. Minimum capitalisation counts premium received on issue only. Investing companies not registered as NBFCs (CICs) need Government approval; NBFC-registered ones are 100% automatic. [SM 305–306]
- **Capital instruments**: equity shares, **fully, compulsorily and mandatorily convertible** debentures and preference shares, share warrants. Partly paid shares: **25%** upfront, the balance within **12 months**. [SM 305]
- Debt converted into equity counts towards the cap; FCCBs and DRs with debt underlying do not. Downstream investment is counted at every stage. [SM 304–307]
- **Start-up convertible notes**: a non-resident may invest **₹25 lakh**; repayable or convertible within **5 years**. [SM 306–308]

### PERMITTED INVESTMENTS BY NON-RESIDENTS (Dec'23 Q8(a)): THE 10 ANNEXES

1. subscribe, purchase or sell capital instruments of an Indian company
2. **FPIs**: listed shares on a stock exchange
3. **NRI/OCI**: listed shares on the exchange, **repatriable**
4. **NRI/OCI**: shares, LLP, firm or proprietorship, **non-repatriable**
5. securities other than capital instruments
6. investment in an **LLP**
7. **FVCI** investment
8. **investment vehicles** (REITs, InvITs, AIFs; not VCFs)
9. issue or transfer to a foreign depository for **depository receipts**
10. **IDRs** of companies resident outside India

Also: rights and bonus issues; **ESOPs and sweat equity** to non-resident employees or directors; shares on merger or demerger; MOA subscription at **face value**. [SM 306–307]

### PRICING · EXIT

- **Issue price not less than:** the **SEBI-guideline price** (listed), or a **fair value by an internationally accepted method**, certified by a CA, SEBI merchant banker or **practising cost accountant** (unlisted). For convertibles, fix the formula upfront; the conversion price is not below the fair value at issue. [SM 307]
- **LLP**: not below fair value certified by a CA, practising cost accountant or approved valuer. [SM 307]
- **Exit**: the Indian partner has the first right of refusal; valuation and capital-gains tax apply. Transfers by foreign-owned Indian companies: to a non-resident (report in **FC-TRS**; no pricing rule) or a resident (pricing rule). [SM 308]

**⚠ REPORTING TIMES (Jun'25 Q8(a), Jun'26 Q7(b)): NOT IN THE SM**

Under the FEMA (NDI) reporting rules: **FC-GPR** within 30 days of **issue** of the shares; **FC-TRS** within 60 days of a transfer or receipt of consideration. Filed on the RBI's **FIRMS** portal after an **Entity Master** registration. Late filing is regularised by paying a **Late Submission Fee**; otherwise it is a contravention (compounding or penalty). The **Jun'26 supplementary** moved **all reporting to FIRMS**, electronic only, with harmonised timelines.

## 6.3 External Commercial Borrowings (ECB) and Trade Credits · Jun'23 Q6(a)(ii), Dec'25 MCQ, PTP Q8(a)

**WHAT IT IS** **ECB** = commercial loans raised by **resident entities from recognised non-resident lenders**, within limits on **minimum maturity, end-use and all-in-cost**, which apply **together**. Governed by s.6 FEMA. [SM 310]

| Parameter | Rule (SM) |
|---|---|
| **Forms** | **FCY ECB**: loans, floating or fixed-rate notes, bonds, debentures (not fully and compulsorily convertible), trade credits beyond **3 years**, FCCBs, FCEBs, financial lease. **INR ECB**: the same plus preference shares and **rupee-denominated bonds issued overseas (masala bonds)** [SM 310] |
| **Eligible borrowers** | **all entities eligible to receive FDI**; INR ECB also micro-finance and non-profit organisations [SM 310] |
| **Lenders** | residents of a **FATF or IOSCO-compliant** country; multilateral and regional institutions; individuals; foreign branches and subsidiaries of Indian banks (FCY ECB only, not FCCB/FCEB) [SM 311] |
| **Minimum average maturity** | **3 years** [SM 311] |
| **Negative end-uses** | **real estate** · **capital market** · **equity investment** · working capital, general corporate purposes, repaying rupee loans (with listed exceptions) · on-lending for these [SM 311] |
| **Limit** | **USD 750 million** (or equivalent) per FY under the **automatic route** (SM MCQ 7 = Dec'25 MCQ). ECB from a **direct foreign equity holder**: ECB liability to equity ≤ **7:1**, unless all ECB is ≤ **USD 5 million** [SM 311] |
| **Special cases** | ECB to repay domestic capex loans classified **SMA-2/NPA** under a one-time settlement; resolution applicants under the IBC repaying the target's rupee loans (**approval route**) [SM 310] |

**PARKING OF ECB PROCEEDS (Jun'23; postal Q5(b); SM essay)**

- **Abroad:** only proceeds meant for **foreign-currency expenditure**, pending use, invested in specified **liquid assets**. [SM 312]
- **In India:** proceeds for **rupee expenditure** are repatriated **immediately** to rupee accounts with **AD Category I** banks, or kept in **term deposits** with them for at most **12 months** cumulatively. [SM 312]

**Procedure:** automatic route if within the parameters; otherwise apply to the RBI. **Reporting:** monthly **ECB-2 Return**. An entity unreachable for **2 quarters**, or without an auditor's certificate for **2 years**, becomes an "**untraceable entity**": no fresh ECB, the ED is informed, no remittance under the automatic route. [SM 312]

**Refinancing:** allowed if the maturity is not reduced and the all-in-cost is lower; Indian banks only for **AAA** companies and Maharatna/Navratna PSUs. [SM 312]

**CONVERTING ECB INTO EQUITY (ICMAI PTP Q8(a))**

1. the activity is under the **FDI automatic route**, or **Government approval** is obtained
2. with the **lender's consent**, at no extra cost, and without breaching the **sectoral cap**
3. **pricing guidelines** complied with
4. **reporting**: partial conversion in **FC-GPR** + ECB-2 marked "partially converted"; full conversion in FC-GPR + ECB-2 "fully converted" (then no more ECB-2); in phases, phase by phase
5. prudential norms of Indian lenders complied with; other lenders' consent or information
6. exchange rate: that on the **agreement date** (or lower, if the lender agrees); fair value as on the **conversion date**

[SM 312–313]

### TRADE CREDITS (TC)

- Buyers' or suppliers' credit for **imports**. Automatic route up to **USD 150 million** per import (oil and gas, airlines, shipping) or **USD 50 million** for others. [SM 313–314]
- Period: up to **3 years** (capital goods); **1 year or the operating cycle**, whichever is less (non-capital goods; shipyards 3 years). [SM 314]
- All-in-cost: benchmark + **300 bps** (new FCY TC), + **350 bps** (old LIBOR-linked), + **250 bps** (INR TC). [SM 314]
- AD reporting: monthly in **Form TC**; quarterly bank-guarantee data on **XBRL**. The **AD ensures compliance**, avoids double financing, and checks the TC period (the role of ADs, an SM essay). [SM 315–316]

### OTHER

- **Security**: ADs may allow charges on assets and guarantees in favour of the overseas lender; entities under restructuring or CIRP only if the resolution plan permits. Entities under FEMA investigation may still raise ECB if otherwise eligible. [SM 313]
- Rupee borrowing between residents is outside FEMA, until a **non-resident guarantee** is invoked. [SM 316]
- **Credit enhancement** by multilateral institutions or foreign equity holders is allowed for rupee bonds of borrowers eligible for automatic-route ECB. [SM 316]

### DEC'26 SUPPLEMENTARY: REVISED ECB FRAMEWORK (FEMA BORROWING AND LENDING AMENDMENT REGS, 2026 · EFFECTIVE 16 FEB 2026)

Simplified and broadened: **all entities eligible to receive foreign investment** may raise ECB · **recognised lenders** realigned · **foreign currency or rupees** · minimum average maturity **generally 3 years** (specific categories differ) · separate cost ceilings rationalised into one **all-in-cost** framework · a **broader permitted end-use**, with specified activities still prohibited. **ICMAI's examination point:** eligible borrowers, recognised lenders, currency, MAMP, all-in-cost, end-uses. [Supp Dec'26 p.7]

The supplementary gives no new limit figure, so the SM's **USD 750 million** remains the figure ICMAI asked (Dec'25, MQP).

## 6.4 Liberalised Remittance Scheme (LRS) · Dec'24 Q7(a)

### WHO · HOW MUCH · WHAT FOR

- **All resident individuals, including minors**, may remit up to **USD 2,50,000 per financial year** (April–March) for permitted **current or capital account** transactions. **Not for** companies, firms, HUFs or trusts. It started on **4 Feb 2004** with USD **25,000**. [SM 317]
- **Purposes:** private visits (not Nepal or Bhutan) · gifts and donations · going abroad for employment · emigration · maintenance of close relatives · business travel, conferences, training, medical check-ups or as an attendant · medical treatment · studies · other current account transactions. [SM 317]
- **Family members** may club remittances, but not for capital account items unless they are co-owners. No limit on the number of remittances, but once USD 2.5 lakh is used, nothing more that year. [SM 318]
- **Remitter:** designate one AD branch; a bank account of at least **1 year**; the AD checks the source of funds; any freely convertible currency. [SM 318]
- A **sole proprietor** has **one** LRS limit, personal and business together. [SM 318–319]

### PROHIBITED · OTHERS

- **Prohibited:** Schedule I items (lottery, sweepstakes, banned magazines) or Schedule II items · **margins** on overseas exchanges · buying **FCCBs** of Indian companies in the secondary market · **forex trading** abroad · capital remittances to **FATF non-cooperative** countries · remittances to persons posing a **terror** risk. [SM 317]
- **Rupee loan to an NRI/PIO close relative:** interest-free, at least **1 year**, within the LRS limit, credited to the **NRO** account, for personal or business use in India, not remitted abroad, and repaid through banking channels. A **rupee gift** to a close NRI relative also counts within the limit. [SM 319]
- **Entities (non-individuals):** donations up to **1%** of forex earnings of the last **3 years** or **USD 5 million** (lower) · commission on property sales **USD 25,000** or **5%** · consultancy **USD 10 million** per infrastructure project, **USD 1 million** others · pre-incorporation expenses **5%** or **USD 100,000** · Schedule III items up to **USD 250,000** a year. More needs **RBI approval**. [SM 319]

### OTHER SUPPLEMENTARY CHANGES (MCQ MATERIAL)

- **FEMA (Guarantees) Regulations, 2026** (6 Jan 2026): a resident generally may **not guarantee a non-resident's debt** except as specifically permitted or with **RBI approval**. The rules set out when Indian entities and non-residents may give guarantees, and how invocation is paid. [Supp Dec'26 p.6]
- **Land-border countries** (1 May 2026): investment where the investor **or its beneficial owner** is in, or a citizen of, a country sharing a land border with India stays on the **Government route**. [Supp Dec'26 p.8]
- **Insurance FDI up to 100%** (2 May 2026), aligned with the insurance-law amendment (see Module 8). [Supp Dec'26 p.8]
- **Jun'26: FIRMS**: all foreign-investment reporting (issue, transfer, downstream) is **electronic on FIRMS**, with harmonised timelines and simpler late-fee regularisation; the investing Indian entity reports downstream investment. [Supp Jun'26 p.7]

## 5 Model answers

**MODEL ANSWER 1 · ISSUING 20% TO A FOREIGN INVESTOR (JUN'23 Q8(b) = SM SOLVED CASE; ALSO ICMAI POSTAL)**

**Facts:** an unlisted company (capital ₹23 crore) in the technology sector, with no foreign-investment cap, plans to issue fresh shares for a **20%** stake to a foreign investor. (i) Is it possible? (ii) What are the steps?

1. **Possible:** yes. Technology is under the **automatic route** with no sectoral cap, so **no prior approval of the Government or RBI** is needed. 20% is within the limit. As the company is unlisted, SEBI's issue regulations do not apply, but **FEMA** does. [SM 305–322]
2. **Price:** not less than **fair value** by an internationally accepted method, certified by a CA, SEBI merchant banker or **practising cost accountant**. [SM 307]
3. **Steps:** Board approval and a **special resolution** for preferential allotment (Companies Act) → receive the money **through banking channels** → allot the shares (**dematerialised**) → **report to RBI** (FC-GPR on FIRMS; ⚠ within 30 days of issue) → same voting rights as others; dividends repatriable after tax. [SM 322]

**MODEL ANSWER 2 · RETURNING RESIDENT'S FOREIGN ASSETS (DEC'25 Q8(a))**

**Facts:** Mr Soni lived in the USA from 2010 to 2024, bought a flat and shares there (USD 100,000), and inherited his wife's US properties (USD 50,000). He returned to settle in India on 1 Jan 2025. May he keep them?

1. **Capital vs current account:** holding a foreign flat and shares is a **capital account** matter, as it concerns a resident's assets outside India (s.2(e)). Current account transactions are trade, services, interest, travel and family maintenance (s.2(j)). [SM 299]
2. **Status:** on returning to settle, he becomes a **person resident in India** (s.2(v)), so s.4 would normally bar holding foreign property. [SM 300–301]
3. **But s.6(4):** a resident may **hold, own, transfer or invest** in foreign currency, foreign securities or **immovable property outside India acquired while he was resident outside India, or inherited from a person resident outside India**. [SM 302]
4. **Conclusion:** he may **keep both**: the flat and shares (acquired while he was non-resident) and the inherited properties (inherited from his wife, a non-resident). Income on them may also be retained, and he may sell or transfer them, **without RBI permission**.

### The SM's own exercise for FEMA (SM 320–322)

| | | | |
|---|---|---|---|
| 1 automatic route means no prior permission of | **RBI or Central Govt** | 7 ECB, automatic route ★ | **USD 750 million** |
| 2 FIIs registered with | **SEBI** | 8 LRS maximum a year | **USD 2,50,000** |
| 3 DPIIT comes under | **Industry and Commerce** | 9 prohibited remittances | **all of the above** |
| 4 a resident selling shares to a non-resident | **capital account** | 10 UK company's shares to a UK citizen | **key: none of the above** ⚠ |
| 5 FDI prohibited in (lottery, gambling, chit funds) | **all of the above** | 11 FEMA … foreign currency transactions | **restricts** |
| 6 LRS purposes | **all of the above** | | |

⚠ MCQ 10: the SM key says "none of the above", but its own fill-in 2 says a security issued by a foreign entity is a **foreign** security (s.2(o)). Prefer "foreign security" if asked. Jun'25 asked the reverse: an Indian company's shares issued to a Singapore resident are **Indian securities**.

**Fill-ins:** FEMA replaced **FERA** · a foreign entity's security is **foreign** · a resident buying a London house is a **capital** account transaction · FEMA is regulated by the **RBI** · WOS = **wholly owned subsidiary** · master directions by the **RBI** · non-capital = **current** account · FCCB converts into the **Indian** company's shares · FPI · RFC = **Resident Foreign Currency** account.

## R Revision: every number in FEMA

| Rule | Number |
|---|---|
| FERA / FEMA in force | 1 Jan 1974 / 1 Jun 2000 |
| FEMA chapters / sections | 7 / 49 |
| Rules (s.46) / Regulations (s.47) | 5 / 23 |
| resident: days in preceding FY | > 182 |
| property held with RBI permission since | 8 July 1947 |
| FDI vs FPI (listed company) | ≥ 10% / < 10% |
| partly paid: upfront / balance within | 25% / 12 months |
| start-up convertible note / within | ₹25 lakh / 5 years |
| FC-GPR after issue ⚠ (not SM) | 30 days |

| Rule | Number |
|---|---|
| ECB automatic route a year | USD 750 mn |
| ECB MAMP / TC beyond … = ECB | 3 yrs / 3 yrs |
| ECB-equity (direct holder) / exempt up to | 7:1 / USD 5 mn |
| parking in India (term deposit) | 12 months |
| untraceable: no reply / no certificate | 2 quarters / 2 years |
| TC per import: oil, air, shipping / others | USD 150 / 50 mn |
| TC period: capital / non-capital | 3 yrs / 1 yr |
| TC all-in-cost spreads | 300 / 350 / 250 bps |
| LRS a year / start (2004) | USD 2,50,000 / 25,000 |
| LRS account age / NRI loan maturity | 1 yr / ≥ 1 yr |
| entity donations | 1% of 3 yrs or USD 5 mn |
| consultancy: infra / other | USD 10 / 1 mn |

# Module 7 · Banking: BR Act, RBI, SARFAESI P13 · Section B · topics 7.1–7.3

SM pp. 323–346 (24 pages). **54.5 marks in 7 papers.** A Banking long question in **every paper** (Q6(b), Q7(b) or Q8(b)), plus an MCQ in 6 of 7 papers, usually on the BR Act. Section numbers the SM does not print are taken from the Act.

| Paper | What was asked | Marks |
|---|---|---|
| Jun'23 | MCQ: no dividend until **capitalised expenses** are written off (= SM MCQ 11) · Q6(b) SARFAESI: **NPA**, **qualified buyer**, **securitisation** | 2 + 8 |
| Dec'23 | MCQ: reserve fund **20%** · MCQ: dividends need **RBI** approval · Q8(b) **ARC measures for asset reconstruction** (SARFAESI s.9) | 2 + 2 + 7 |
| Jun'24 | MCQ: bank amalgamation needs **two-thirds** (= SM MCQ 8) · Q7(b) **restrictions on loans and advances** (s.20, 21) | 2 + 5 |
| Dec'24 | MCQ: SARFAESI judicial authority = **DRT** (= SM MCQ 7) · Q6(b)(ii) **disposal of non-banking assets** (BR Act s.9: not in the SM) | 2 + 3 |
| Jun'25 | MCQ: winding up is ordered by the **High Court** · Q5(b)(ii) SARFAESI **s.15 takeover of management** | 2 + 3.5 |
| Dec'25 | Q8(b) **role of the RBI** in monetary, banking and financial policy | 7 |
| Jun'26 | MCQ: **s.6** businesses: all of the above · Q8(b) **SARFAESI**: objectives, applicability, s.13 enforcement, secured creditors' rights | 2 + 7 |

**HOW IT IS EXAMINED · DEC'26 PREDICTION**

- Answers are **SM lists**: s.20/21, the RBI's roles, SARFAESI s.9, s.13 and s.15. MCQs: SM exercise MCQs or single SM sentences.
- **Q8(b), 7 marks**: (1) **loans and advances s.20/21** (rotation; about 40%); (2) **ARC measures s.9** (PTP Q8(b); 30%); (3) **role of the RBI** (MQP Q8(b), postal; 20%). The SM solved case (**MD of a bank**) is a good case-study candidate.
- MCQ: s.15, s.17 (20%), s.44A (2/3), CRR/SLR, the DRT.

**MAP**

1. BR Act: s.6 business, board, chairman ★★
2. Capital, dividend s.15, reserve s.17, CRR/SLR ★★★
3. Loans s.20/21, licensing s.22, s.9 ⚠ ★★★
4. RBI powers, winding up, amalgamation s.44A ★★
5. Role of the RBI (18 roles) ★★
6. SARFAESI: definitions, ARCs, s.9, s.13, s.15 ★★★
7. Model answers · SM exercise · numbers

## 7.1 Banking Regulation Act, 1949: business and management · Jun'26 MCQ

Banking is in **entry 45 of the Union List**. The Act regulates all banking companies and supplements the Companies Act; **primary agricultural credit societies** and **cooperative land mortgage banks** are excluded. It empowers the RBI to **license** banks, regulate shareholding and voting, supervise boards and management, regulate operations, direct audits, impose a **moratorium**, handle mergers and liquidation, issue directions and impose penalties. [SM 325]

**s.6 · WHAT A BANKING COMPANY MAY DO**

SM WORDS **"Banking"** means accepting, for the purpose of lending or investment, of **deposits of money** from the public, **repayable on demand or otherwise** and **withdrawable by cheque, draft, order or otherwise**. A banking company is any company which transacts the business of banking. [SM 325]

In addition to banking it may: (a) act as **agent for any Government**, local authority or person (not as managing agent); (b) underwrite and deal in issues of loans and securities; (c) **guarantee and indemnity** business; (d) **manage, sell and realise property** received in satisfaction of its claims; (e) deal in property held as security; (f) **undertake and execute trusts**; (g) administer estates as **executor or trustee**; (h) set up funds for employees; grant money for charity; (i)–(j) build, manage and deal with its own property; (k) take over a similar business; (l) incidental acts; (m) any other business the **CG** specifies. *Jun'26 MCQ: (D) all of the above.* [SM 325–326]

**BOARD · CHAIRMAN (s.10A, 10B, 10BB)**

- At least **51%** of the board must have special knowledge or experience: accountancy, agriculture and rural economy, banking, co-operation, finance, law, small-scale industry, or another field the RBI approves; at least **two** from agriculture and rural economy, co-operation or SSI. [SM 326]
- Directors other than the chairman and whole-time directors hold office for at most **8 years**. No conflicts of interest; the RBI may order the board **reconstituted**; **no common directors** across banks. [SM 326]
- **s.10B**: the board names one director as **Chairman**, whole-time or part-time. A whole-time chairman manages the whole affairs under the board's supervision; with a part-time chairman, a **Managing Director** manages. Both need **RBI approval**, for at most **5 years** at a time. [SM 326]
- **s.10BB**: if the post of whole-time chairman or MD is vacant and that harms the bank, the **RBI may appoint** a fit person (term up to **5 years**), who is deemed a director. [SM 326]

## s.11–19 Capital, dividend, reserve fund, CRR · Jun'23, Dec'23 MCQs

### CAPITAL (s.11, 12)

- **Subscribed capital ≥ half of authorised**; **paid-up ≥ half of subscribed**; on an increase, up to **two years** to restore the ratio. Shares may be equity or preference. [SM 327]
- No person may exercise more than **10%** of voting rights, which may be raised to **20%** in phases (SM). [SM 327] ⚠ The Act (2012 amendment) lets the RBI raise the cap up to 26%, which it did in 2016.
- **Basel III**: three pillars, namely minimum capital on **risk-weighted assets** (credit, market, operational risk), **supervisory review**, and **market discipline** (disclosures); capital buffers; compliance from **1 Jan 2019**, with total capital of at least **9%** of RWAs. [SM 327]

### DIVIDEND (s.15) · JUN'23 MCQ = SM MCQ 11

SM WORDS No banking company shall pay any dividend on its shares until all its **capitalized expenses** (preliminary expenses, brokerage and commission on issue of shares, etc.) have been **completely written off**. It may pay **without** writing off: (a) depreciation on **approved securities** not capitalised or treated as a loss; (b) depreciation on other investments that is **adequately provided** (auditor approves); (c) **bad debts** adequately provided (auditor approves). (d) Banks pay dividends after **specific approval of the RBI** (Dec'23 MCQ). [SM 327]

### RESERVE FUND (s.17) · DEC'23 MCQ

- Every bank incorporated in India transfers **at least 20% of profit** each year to the reserve fund, until the fund plus **share premium** equals the **paid-up capital**; the CG may exempt on the RBI's recommendation. [SM 328]
- Any appropriation from reserves is reported to the RBI within **21 days**, with reasons. [SM 328]
- RBI directive: scheduled commercial banks (incl. foreign banks) transfer at least **25%** of net profit. [SM 328]

### CASH RESERVE (s.18) · SUBSIDIARIES (s.19)

- A **non-scheduled** bank keeps a daily cash reserve of at least **3%** of its time and demand liabilities (with itself, or in a current account with the RBI, SBI or a notified bank) and reports by the **20th** of each month. **Scheduled** banks' CRR is under **s.42 of the RBI Act, 1934**. [SM 328]
- **s.19**: a bank may form subsidiaries only for permitted or incidental purposes, with the RBI's prior written permission; it may not take controlling interests in non-banking companies. [SM 328]

## s.20–30 Loans, licensing, branches, liquidity, returns · Jun'24 Q7(b), Dec'24 Q6(b)(ii)

### RESTRICTIONS ON LOANS AND ADVANCES (s.20, 21) · THE JUN'24 ANSWER

SM WORDS **Section 20** restricts banking companies from granting any loan to (i) any of its **directors**, (ii) any **firm in which a director is interested**, or (iii) any individual for whom a **director stands as guarantor**. Banks are also prohibited from granting loans or advances **on the security of their own shares**. The RBI may control advances by any bank in the public interest. [SM 328]

**Section 21**: the RBI determines the **policy on advances** and may direct banks on: (a) the **purposes** for which advances may or may not be granted; (b) the **margins** on secured advances; (c) the **rate of interest** on advances, other accommodation and commission on guarantees; (d) the **maximum amount** of advances or guarantees for a **single party**, having regard to the bank's paid-up capital, reserves and deposits. [SM 328]

#### ⚠ DISPOSAL OF NON-BANKING ASSETS (s.9): DEC'24 Q6(b)(ii), NOT IN THE SM

From the Act: a banking company shall **not hold any immovable property**, however acquired, **except what it needs for its own use**, for more than **seven years** from its acquisition, and must **dispose of it** within that period. The **RBI may extend** the period by up to **five years** if that is in the depositors' interest. (Property received in satisfaction of claims, s.6(d), is the usual source.)

### LICENSING (s.22) · SM ESSAY 2

- No banking company may **commence or carry on banking** in India without an **RBI licence**. [SM 328]
- Before licensing, the RBI may **inspect the books** and must be satisfied that: (1) it can **pay depositors in full**; (2) its affairs will **not be run against depositors' interests**; (3) for a foreign bank, it is in the **public interest** and its home country does **not discriminate** against Indian banks. [SM 329]
- **Cancellation** if it stops banking in India or breaks licence conditions; **appeal to the CG within thirty days**, whose decision is final. [SM 329]
- RRBs are under the **RRBs Act 1976**. Licences are "**on tap**" (2016 guidelines); in 2015 Bandhan Bank and IDFC Bank got licences. [SM 329]

### OTHER CONTROLS

- **s.23** branches: no new place of business in or outside India, and no change of place, without the **RBI's prior permission**; not needed for a **temporary** place (up to **1 month**) for an exhibition, conference or mela. [SM 329]
- **s.24 SLR**: liquid assets (cash, gold, unencumbered approved securities) of up to **40%** of time and demand liabilities, as the RBI notifies. [SM 329]
- **s.25**: assets in India of at least **75%** of its demand and time liabilities in India, at the last Friday of each quarter. [SM 330]
- **s.26**: return of accounts **un-operated for 10 years**, within **30 days** after each calendar year. **s.27**: monthly return of assets and liabilities. [SM 330]
- **s.30 audit**: accounts audited; **RBI's prior approval** to appoint, re-appoint or remove auditors; **three copies** to the RBI within **three months**. [SM 330]

## s.35–44A RBI's powers, moratorium, winding up, amalgamation · Jun'24, Jun'25 MCQs

- **s.35A directions**: the RBI may caution or prohibit banks, or issue binding directions, in the **public interest**, in the interest of **banking policy**, to protect **depositors**, or to secure proper management. [SM 330]
- The **CG may authorise the RBI** to direct banks to start **insolvency resolution under the IBC** for a default; the RBI may issue directions on **stressed assets** (s.35AB). [SM 330–331]
- **s.35B**: **RBI's prior approval** for the number of directors, and for appointment, re-appointment, remuneration and removal of the chairman, MD or a director; also for amendments to the MOA, AOA or resolutions on these matters. [SM 331]
- **s.36AA, 36AB**: the RBI may **remove managerial persons** and **appoint additional directors**. The board may be **superseded**; the CG may **acquire** the undertaking (s.36AE). [SM 331]
- **s.37 moratorium**: a bank temporarily unable to pay may ask the **High Court** to stay all proceedings for up to **6 months**, with an **RBI report** that it can pay its debts if granted. [SM 331]
- **Winding up (s.38–44)**: the **High Court** orders it (Jun'25 MCQ: (D)) if the bank cannot pay its debts or the RBI applies. [SM 331]
- **RBI may apply** if the bank: (a) fails the s.11 **capital** requirement; (b) has **no licence** under s.22; (c) is **barred from taking deposits**; (d) keeps breaking the Act after RBI notice; (e) a court-sanctioned compromise **cannot work**; (f) per its returns, **cannot pay its debts** or its continuance harms depositors. [SM 331]
- **Voluntary winding up** only if the RBI certifies it can pay its debts **in full**. The **CG may acquire** a banking company by compulsory transfer of shares (an SM fill-in). [SM 331–332]
- **Amalgamation (s.44A)**: the scheme is approved by a majority of **2/3 in value** of the shareholders of **each** company, present in person or by proxy (Jun'24 MCQ = SM MCQ 8). Dissenters get the value of their shares **as determined by the RBI**. The **RBI sanctions** the scheme, directs the transfer of assets and liabilities and dissolves the transferor bank. Since **October 2020** the RBI may start reconstruction or amalgamation **without a moratorium**. [SM 332]

## 7.2 Role of the Reserve Bank of India · Dec'25 Q8(b), MQP Q8(b), postal Q6(a)

**SM WORDS** Since its inception the Reserve Bank has been playing a **key role in the formulation of monetary, banking and financial policies**, moving from **"regulator" to "facilitator"**. [SM 333]

| # | Role | What the SM says |
|---|---|---|
| i | **Inspection of banks** | under the BR Act, in the interest of the banking system, banking policy and depositors [SM 333] |
| ii | **Regulating commercial banks** and LABs | Department of Banking Operations and Development: licensing, branch expansion, liquidity reserves, management, amalgamation, reconstruction and liquidation |
| iii | **Anti-money laundering** | AML cell for combating financing of terrorism (CFT) under the PMLA (SM fill-in 8) |
| iv | **Board-level appointments** | approves private banks' chairmen, MDs and CEOs; recommends PSB executive directors, CMDs, non-official and RBI nominee directors to the Government |
| v | **Licensing of branches** | authorisations, complaints on opening or closing offices, periodic policy review, branch and ATM database |
| vi | **Banking policy** (prudential norms) | capital adequacy; income recognition, asset classification and provisioning; investment valuation; exposure limits; PSB capital; Basel II; ALM; NPA settlements; FCRA donations [SM 334] |
| vii | **Directives to banks** | deposit interest rates (incl. NRI), deposit accounts, agents, gifts, freezing of accounts; capital-market exposure |
| viii | **Information on defaulters** | borrowers with dues of **₹1 crore and above** classed doubtful or loss, half-yearly (31 March, 30 September) [SM 334] |
| ix | **Indian banks abroad** | branches, JVs, representative offices; management and correspondent agreements |
| x | **Precious metals** | gold deposit and import schemes; authorising banks to import gold, silver, platinum |
| xi | **Offshore banking units** | OBUs in **SEZs**; IFSCs (SM fill-in 6) [SM 334–335] |
| xii | **Industrial and export credit** | policy, export credit and industrial rehabilitation desks |

| | | |
|---|---|---|
| xiii–xiv | **Interpretation · exemptions** | interprets the BR and RBI Acts; frames rules; grants exemptions |
| xv | **Foreign exchange (FEMA)** | permissions; capital-account conditions (s.6(2)), regulations (s.6(3)); export realisation (s.8); exemptions (s.9); authorised persons (s.10–12). It **cannot restrict current-account transactions**; only the CG can, in consultation with the RBI [SM 335] |
| xvi–xviii | **Bankers' bank · Government's banker · payments** | lends to banks; banker to the Central and State Governments and issues their bonds; oversees payment and settlement systems [SM 335] |

## 7.3 SARFAESI Act, 2002 · Jun'23 Q6(b), Dec'23 Q8(b), Jun'25, Jun'26 Q8(b)

### PURPOSE (SM ESSAY 5) · JUN'26 "OBJECTIVES"

- In force from **21 June 2002** (amended 2004, 2012), to regulate **securitisation** and **reconstruction of financial assets** and **enforcement of security interest**. [SM 336]
- It lets banks and FIs **realise long-term assets**, manage liquidity and asset-liability mismatch and **improve recovery** by taking possession of securities and selling them, reducing **NPAs**. [SM 336]
- It promotes **asset reconstruction companies** to take over NPAs, and gives lenders and ARCs power to take over assets **without first going to court**. [SM 336]

### DEFINITIONS · JUN'23 Q6(b) (3 + 3 + 2)

- SM WORDS **Non-performing asset**: an asset or account of a borrower classified by a bank or FI as **sub-standard, doubtful or loss**, (a) per the directions of the authority that regulates that bank or FI, or (b) otherwise per the **RBI's** asset-classification directions. [SM 337]
- **Qualified (institutional) buyer**: an FI, insurer, bank, SFC, SIDC, trustee, **ARC** registered under s.3(4), an **AMC investing for a mutual fund** or pension fund, a **SEBI-registered FII**, or any body corporate specified by SEBI. [SM 337]
- **Securitisation**: **acquisition of financial assets** by an ARC from any originator, by raising funds from qualified buyers through **security receipts** representing undivided interests in those assets, or otherwise. [SM 338]
- **Asset reconstruction**: acquisition by an ARC of a bank's or FI's rights in a financial assistance **for its realisation**. **Borrower** includes a guarantor and a mortgagor. **Default**: non-payment leading to NPA classification; for debt securities, after a **ninety days** notice. [SM 336–337]

### ASSET RECONSTRUCTION COMPANIES (s.3–11)

- **Registration with the RBI** (SM MCQ 6) and **owned fund** of at least **₹2 crore** or more as the RBI specifies. [SM 338] ⚠ The RBI's 2022 framework requires ₹300 crore.
- Conditions: no losses in the **three preceding years**; arrangements to realise assets and pay investors; experienced directors; no director convicted of moral turpitude; a fit and proper sponsor; prudential norms. RBI approval for a **substantial change in management**, registered office or name. [SM 338]
- **Cancellation (s.4)**: stops holding qualified-buyer investment or doing the business; breaks conditions or directions; does not keep accounts or submit to inspection; after an opportunity to comply. [SM 338–339]
- **Acquisition (s.5)**: by issuing debentures or bonds, or by agreement with the bank; such documents are **exempt from stamp duty**. [SM 339]
- **s.10**: an ARC may act as a bank's **agent** for recovery, as a **manager** under s.13(4)(c), or as a court-appointed **receiver**; no other business without RBI approval. **s.11**: disputes among banks, ARCs and buyers go to **conciliation or arbitration**. [SM 339–340]

### s.9 · MEASURES FOR ASSET RECONSTRUCTION (DEC'23 Q8(b), PTP)

a. proper management of the borrower's business by **change in or takeover of management**
b. **sale or lease** of part or whole of the business
c. **rescheduling** of payment of debts
d. **enforcement of security interest** under the Act
e. **settlement of dues**
f. **taking possession** of secured assets
g. **conversion of debt into shares** of a borrower company (deemed always valid)

The **RBI** sets the policy and gives directions, including on management of the borrower's business and fees. [SM 339]

### s.13 · ENFORCEMENT WITHOUT A COURT (JUN'26 Q8(b))

1. A security interest may be enforced **without the intervention of a court or tribunal**. [SM 340]
2. Borrower defaults and the account is classified an **NPA** → written **notice to pay in full within sixty days**, giving the amount and the assets to be enforced. [SM 340]
3. The creditor considers any objection and replies with reasons within **fifteen days**. [SM 340]
4. **Measures (s.13(4))**: (a) **take possession** of secured assets, with the right to lease, assign or sell; (b) **take over management** of the business (transfer only where a substantial part of the business is security); (c) appoint a

### s.15 · TAKEOVER OF MANAGEMENT (JUN'25 Q5(b)(ii))

- The ARC or secured creditor may appoint as many **directors** (company) or **administrators** (others) as it thinks fit, and **publishes a notice** in an **English** and an **Indian-language** newspaper where the principal office is. [SM 342]
- **Effect**: the existing directors or administrators are **deemed to vacate office** and their **contracts end**; shareholders cannot appoint directors without the creditor's approval; **no winding-up** or receiver proceedings without its consent. Management is **restored** once the debt is realised in full. [SM 342]

**manager**; (d) require anyone who owes the borrower money to **pay the creditor**. [SM 340]

5. A transferee gets **good title**; proceeds go first to costs, then to the creditor's dues, residue to the borrower. If the borrower **tenders the full dues** before the auction notice, the asset cannot be sold. [SM 341]
6. **Consortium**: action needs creditors with at least **60% in value**, binding on all. A shortfall can be recovered through the **DRT**; guarantors and pledged assets may be pursued directly. After notice, the borrower may **not transfer** the secured assets except in the ordinary course. [SM 341–342]

- **s.16**: no **compensation** to directors or managers for loss of office. [SM 342]

**APPEALS**

- **s.17**: an aggrieved borrower or person appeals to the **DRT** (the "judicial authority": Dec'24 MCQ = SM MCQ 7). [SM 342] Act: within 45 days.
- **s.18**: against the DRT's order, to the **Appellate Tribunal within thirty days**; the borrower must deposit **50%** of the debt (claimed or determined, whichever is less), reducible to **25%**. [SM 342]

**⚠ APPLICABILITY (s.31): JUN'26 ASKED IT; NOT IN THE SM**

From the Act, the enforcement provisions do **not** apply to: a **lien** on goods or money; a **pledge of movables**; security on **aircraft** or **vessels**; a financial asset of **₹1 lakh or less**; **agricultural land**; cases where the amount due is **less than 20%** of the principal and interest. Secured creditors covered: banks, FIs, ARCs, debenture trustees, and notified NBFCs.

## M Model answers

**MODEL ANSWER 1 · SARFAESI: OBJECTIVES, APPLICABILITY, ENFORCEMENT, RIGHTS (JUN'26 Q8(b)) · 7 MARKS**

(1) **Objectives**: the three points of "Purpose" above. (2) **Applicability**: secured creditors (banks, FIs, ARCs) against borrowers whose account is an **NPA**; the exclusions of s.31 (⚠ box). (3) **Enforcement (s.13)**: no court needed; **sixty days** notice; reply to objections in **fifteen days**. (4) **Rights and measures**: take **possession** and sell, lease or assign; take over **management** (s.15); appoint a **manager**; collect from the borrower's debtors; **60%** consortium rule; recover any shortfall via the **DRT**; pursue guarantors. (5) **Borrower's remedy**: DRT (s.17), then the Appellate Tribunal with a **50%** deposit. [SM 336, SM 340–342]

**MODEL ANSWER 2 · SM SOLVED CASE: APPOINTING THE CFO AS MD OF A LISTED BANK**

**Facts:** the MD of a large listed bank is retiring; the NRC finds the CFO, a CA, suitable. **Steps:** (1) **Companies Act**: the **NRC recommends** → the **Board appoints** the MD → approval at the next **general meeting**. (2) **BR Act** also applies: the MD of a bank is appointed with the **prior approval of the RBI** (s.10B; also s.35B, which covers appointment, re-appointment, remuneration and removal), for up to **5 years** at a time. **So RBI approval must be obtained** before the appointment takes effect. [SM 326, SM 331, SM 345–346]

**The other past long questions are SM lists printed above:** s.20/21 (Jun'24 Q7(b)) · SARFAESI s.9 (Dec'23 Q8(b)) · role of the RBI, (i)–(xviii) (Dec'25 Q8(b): write 8–10 roles, each with a line) · s.15 takeover (Jun'25) · NPA, qualified buyer, securitisation (Jun'23).

### The SM's own exercise for Banking (SM 343–346)

| | | | |
|---|---|---|---|
| 1 NPA stands for | **(b)** "Non Performance Asset" (key; really non-*performing*) | 7 SARFAESI judicial authority ★ | **DRT** |
| 2 BR Act enacted in | **1949** | 8 bank amalgamation vote ★ | **two-thirds** |
| 3 cash reserve ratio | **4%** (key) ⚠ | 9 liquid assets at least | **25%** (key) ⚠ |
| 4 SLR stands for | **(b)** (key; really statutory liquidity *ratio*) | 10 balance sheet as on last working day of | **accounting year** |
| 5 written off before dividend | **all of the above** | 11 no dividend until ★ | **capitalised expenses** written off |
| 6 ARCs registered with | **RBI** | | |

⚠ MCQ 3: the SM text gives **3%** for non-scheduled banks (s.18); the key's 4% was the RBI's CRR for scheduled banks when the SM was written (cut to 3% by Nov 2025). MCQ 9: the key's 25% is the old statutory floor; s.24 now says "up to 40%, as the RBI notifies". In the exam, pick the option that matches the question's wording.

**True/False:** NBFCs come under the BR Act **F** · RBI approval for a bank's MD **T** · no dividend until capitalised expenses are written off **T** · RBI can cancel a licence without notice **F** · non-scheduled banks' CRR is outside the BR Act **F** (it is s.18). **Fill-ins:** licence by the **RBI** · Basel **III** from Jan 2019 · SLR = **statutory liquidity ratio** · **CG** can acquire shares of any bank in the public interest · LAB = **local area bank** · OBU = **offshore banking unit** · **CG** may acquire a banking company · CFT = **combating financing of terrorism**.

## R Revision: numbers

| Rule | Number | Rule | Number |
|---|---|---|---|
| board with special knowledge / agri etc. | ≥ 51% / ≥ 2 | assets in India (s.25) | ≥ 75% |
| director tenure / chairman, MD approval | 8 yrs / 5 yrs | un-operated accounts / return | 10 yrs / 30 days |
| subscribed ≥ ½ authorised; paid-up ≥ ½ subscribed | 2 yrs to restore | accounts to RBI (s.30) | 3 copies / 3 months |
| voting cap (SM) | 10% → 20% | s.37 moratorium | ≤ 6 months |
| Basel III total capital | 9% from Jan 2019 | amalgamation (s.44A) | 2/3 in value |
| reserve fund (s.17) / RBI for SCBs | 20% / 25% | licence appeal to CG | 30 days |
| reserve appropriation reported | 21 days | defaulter data (RBI) | ≥ ₹1 crore |
| CRR non-scheduled / report by | 3% / 20th | SARFAESI notice / reply | 60 / 15 days |
| SLR ceiling (s.24) | 40% | consortium consent | 60% in value |
| temporary branch | 1 month | DRAT appeal / deposit | 30 days / 50% (min 25%) |
| non-banking assets (Act) | 7 yrs + 5 | ARC owned fund (SM) / no losses in | ₹2 cr / 3 yrs |

# Module 8 · Insurance Act, 1938 and IRDA Act, 1999 P13 · Section B · topics 8.1–8.2

SM pp. 347–368. **22.5 marks in 7 papers**: an Insurance **MCQ in 6 of 7 papers** (none in Jun'26), and short long-question parts on **indemnity and subrogation** and **IRDA's objectives**. The **Sabka Bima Sabki Raksha Act, 2025** (Dec'26 supplementary) is the big change.

| Paper | What was asked | Marks |
|---|---|---|
| Jun'23 | MCQ: minimum paid-up capital for life insurance = **₹100 crore** (= SM MCQ 1) | 2 |
| Dec'23 | MCQ: a promise that something shall or shall not be done, or a condition fulfilled = **warranty** | 2 |
| Jun'24 | MCQ: ₹100 crore again · Q7(a) principles of **indemnity and subrogation** | 2 + 5 |
| Dec'24 | MCQ: a policy cannot be questioned after **3 years** (s.45; = SM MCQ 6) · MCQ: when **insurable interest** must exist | 2 + 2 |
| Jun'25 | MCQ: **3 years** again · Q7(b)(ii) **objectives of setting up IRDA** | 2 + 3.5 |
| Dec'25 | MCQ: IRDA's annual report to the CG within **nine months** (= SM MCQ 12) | 2 |
| Jun'26 | nothing | 0 |

**HOW IT IS EXAMINED · DEC'26 PREDICTION**

- **MCQ (xiii)–(xv): about 55%**, the most likely "other law" MCQ. The 2025 amendment gives new MCQ facts: **FDI 100%**, **5%** share-transfer threshold, **₹1,000 crore** NOF for foreign reinsurers.
- Repeating MCQs: ₹100 crore, 3 years, nine months, insurable interest. A long part (3–5 marks) on principles or IRDA is possible but rare.

**MAP**

1. History, FDI ⚠ ★★
2. Principles: good faith, warranty, indemnity, subrogation, insurable interest ★★★
3. Insurance Act: capital, accounts, investments, agents, s.45 ★★★
4. IRDA: objectives, functions, constitution ★★
5. 2025 amendment · SM exercise · numbers

## 8.1 History and foreign investment

- Before **1912** there was no insurance law (the Companies Act 1882 applied). **1912**: the Indian Life Insurance Companies Act and the Provident Insurance Societies Act (life only). The **Insurance Act, 1938** came into force on **1 July 1939**; amended comprehensively in **1950**. [SM 349]
- Life insurance nationalised in **1956**: **LIC** from **1 September 1956** (SM fill-in 6). Marine Insurance Act **1963**. General insurance nationalised in **1972**. [SM 349]
- On the **Malhotra Committee** report, the sector opened to private players in **2000** with the **IRDA Act, 1999**; before that only LIC and GIC (with four subsidiaries). [SM 349]

**⚠ FDI: THE SM IS TWO CHANGES BEHIND**

SM: up to **26%** automatic, up to **49%** with CG approval; **100%** in intermediaries (brokers, consultants). [SM 349] It went to 74% (2021), and the **Sabka Bima Sabki Raksha Act, 2025** raised it to **100%** (FEMA NDI Rules aligned on **2 May 2026**). [Supp Dec'26 p.8]

## 8.1.3 Principles of insurance · Jun'24 Q7(a), Dec'23, Dec'24 MCQs

- **Utmost good faith**: insurance is a contract **uberrimae fidei**; both parties must disclose every material fact (*General Assurance Society v. Chandumull Jain*, SC 1966) (an SM fill-in). [SM 350]
- **Misrepresentation**: representations are statements outside the contract; made part of it, they become warranties. To prove it **wilful**: (a) a material matter, (b) suppressed fraudulently, (c) the holder knew it was false. [SM 350] ⚠ The SM's "two years" here is the old s.45; it is now three years (below).
- **Warranty** (Dec'23 MCQ): a breach **avoids the policy even if not material** to the risk; express or implied (implied mostly in marine). [SM 350]
- **Indemnity** (Jun'24): except **life and personal accident**, policies are contracts of indemnity: the insurer pays the **actual loss**, never more (*Vania Silk Mills*, 1991). Limits: (a) the loss must be **proved**; (b) at most the **sum in the policy**; (c) only **proximate** causes; (d) **market value** governs (SM MCQ 17: any or all). [SM 351]
- **Subrogation** ⚠ (the SM gives only the heading): once the insurer **pays the loss**, it **steps into the shoes of the insured** and takes over his rights and remedies against third parties who caused the loss, **up to the amount paid**. It follows from indemnity: the insured cannot recover twice. **Contribution**: with several insurers on the same risk, each bears a rateable share, so the insured does not profit (SM MCQ 13).

- **Conditions**: **precedent** (not met → void ab initio) or **subsequent** (breach → avoided from then); implied conditions (insurable interest, good faith). A condition cutting the limitation period is **void**; an insurer cannot rely on a condition not in the policy (*Modern Insulators*, 2000). [SM 350]
- **Proximate cause** (*causa proxima non remota spectatur*): pay only for loss caused directly by the insured peril; the insured proves it. [SM 351]
- **Insurable interest**: a relationship in which the event would cause the insured **pecuniary loss**; without it the contract is a **wager and void**. Creditors (in the debtor) and employees (in the employer) have it. [SM 351–352]
- **When must it exist? Life and personal accident**: at the **time of taking the policy**. **Fire and motor accident**: **both** at the policy and at the accident (SM MCQ 18). **Marine**: not needed when taking the policy. [SM 352] *Dec'24 MCQ lumped "life and motor" together; the motor rule (C) is the stricter SM sentence.*
- **Consumer protection**: insurance services are covered, so policyholders may complain; an **insurer is not a "consumer"** even by subrogation (*New India Assurance v. B.N. Sainani*, 1997). [SM 351]

## 8.1.4 Insurance Act, 1938: definitions and salient provisions · Jun'23, Jun'24, Dec'24, Jun'25 MCQs

**Definitions**: **Insurer** = an Indian insurance company, a statutory insurer, an insurance **co-operative**, or a **foreign reinsurer's branch** (incl. Lloyd's). **Indian insurance company**: a public company limited by shares, solely for life, general, health or re-insurance business, with foreign holding within the limit (SM: **49%**). **General insurance** = fire, marine or miscellaneous. **Re-insurance** = insurance of part of one insurer's risk by another for a premium (SM fill-in 2). **Controller of Insurance** = the officer the **CG** appoints to exercise the Authority's powers (SM MCQ 3). [SM 352–353]

| Provision | Rule (SM) |
|---|---|
| **s.2CB** foreign insurers | no policy on property in India, or on an Indian ship or aircraft, with an insurer based abroad **without IRDAI permission** [SM 354] |
| **s.6 capital** ★ | minimum paid-up capital: **life or general ₹100 crore**; **health ₹100 crore**; **reinsurance ₹200 crore** (Jun'23, Jun'24 MCQ = SM MCQ 1, 9). Equity shares of one face value; votes only on equity; same paid-up amount on all shares. "Net owned funds of not less than ₹5,000 crore" [SM 354] ⚠ that NOF applies to foreign reinsurers' branches, and the 2025 Act cut it to ₹1,000 crore. |
| **s.12, 15** accounts | audited accounts and statements, printed, **four copies** to the Authority within **six months** [SM 354–355] |
| **s.13** actuarial valuation | life insurers: investigation and valuation of liabilities **at least once a year** (SM MCQ 5) [SM 355] |
| **s.14** records | record of **policies** (holder, date, assignments, nominations) and of **claims** (date, claimant, settlement or rejection with reasons); may be electronic [SM 355] |
| **s.27** investments | life: **25%** in Government securities + a further **twenty-five per cent** in Government or approved securities, balance in approved investments. General: **25%** in Government securities + **ten per cent** more (SM MCQ 4). In **promoter-group** companies: at most **five per cent** (s.27C) [SM 355–356] |
| **s.29, 30** loans | no loans to the insurer's **directors, manager, actuary, auditor or officers** or their firms, except policy loans within surrender value; directors party to a breach of s.27–29 are **jointly and severally liable** for the loss [SM 356] |
| **s.32D** motor third party | general insurers underwrite a minimum share of **motor third-party** business; penalty up to **₹25 crore** (s.105B) [SM 356] |
| **s.33** investigation | the Authority may investigate any insurer or intermediary at any time; costs borne by the insurer, recoverable as land revenue [SM 356] |
| **s.40, 42** agents | commission only to **agents or intermediaries**, per regulations. An agent may act for at most **one life, one general, one health insurer** and one of each mono-line insurer; no principal, chief or special agents; **no multi-level marketing**; no agent may be a director of an insurer without permission [SM 356–357] |
| **s.45** ★★ | no life policy can be called in question **on any ground** after **3 years** from the date of the policy (Dec'24, Jun'25 MCQ = SM MCQ 6 and a fill-in). Within 3 years it may be questioned for **fraud** or **material mis-statement or suppression**, the insurer stating the grounds in writing [SM 357] |

| | |
|---|---|
| **s.64UM** surveyors | must hold prescribed qualifications and be members of the **Indian Institute of Insurance Surveyors and Loss Assessors**; follow a code of conduct [SM 357] |
| **s.64V** valuation and solvency | assets at no more than **market or realisable value**; statement certified by an approved auditor or actuary as on **31 March**. Assets must exceed liabilities by at least **fifty per cent** of the s.6 minimum capital; otherwise the insurer is **deemed insolvent** and may be wound up [SM 357–358] |

**SABKA BIMA SABKI RAKSHA (AMENDMENT OF INSURANCE LAWS) ACT, 2025 (DEC'26 SUPPLEMENTARY)**

Assent **20 December 2025**; in force **5 February 2026** (except s.25). Amends the Insurance Act, the IRDAI Act and related laws: (1) **foreign investment** in an Indian insurance company raised from **74% to 100%**, subject to conditions; (2) prior approval for a **transfer of shares** needed above **5%** (was 1%); (3) **net owned funds of foreign reinsurers** cut from **₹5,000 crore to ₹1,000 crore**. [Supp Dec'26 p.8, Supp Dec'26 p.9]

## 8.2 IRDA Act, 1999 · Jun'25 Q7(b)(ii), Dec'25 MCQ, postal Q7(a)

### OBJECTIVES (JUN'25) · MISSION

Set up in **1999** (SM MCQ 8) with the objectives: (i) to **protect the interests of policyholders**; (ii) to **regulate, promote and ensure orderly growth** of the insurance industry; (iii) connected matters. [SM 359]

**Mission**: (i) protect policyholders and secure their **fair treatment**; (ii) **speedy and orderly growth** for the common man, and long-term funds; (iii) high standards of **integrity, financial soundness and fair dealing**; (iv) act where standards are weak; (v) **speedy settlement of genuine claims**, prevent fraud, grievance machinery; (vi) optimum **self-regulation**. [SM 359]

### FUNCTIONS AND POWERS (s.14)

Policies and regulations on: nomination; claim settlement; training of agents; insurable interest; surrender value; codes of conduct; policy information; MIS; self-regulation; **registration certificates** (issue, modify, cancel); **investment of funds**; **solvency margin**; supervising insurers; qualifications of agents; fees; **investigations**; **adjudicating disputes** between insurers and intermediaries; business outside the Tariff Advisory Committee. [SM 359–361]

### CONSTITUTION

- A body corporate; **Chairperson**, up to **five whole-time** and up to **four part-time** members, experts in insurance, law, economics, accountancy, actuarial science. [SM 360]
- Chairperson: **five years** or till **sixty-five**, re-appointable (SM MCQ 10); whole-time members till **sixty-two**. Resignation on **three months'** notice; removal for insolvency, insanity, moral-turpitude conviction, conflicting interest. No Government or insurance job for **two years** after leaving. Decisions by majority; chair has a casting vote. [SM 360]
- **Fund**: Government grants, fees and charges, other sums (SM MCQ 11), used for salaries and expenses; accounts audited by the **CAG** and laid before Parliament. [SM 361]
- **Amalgamation or transfer** of insurance business only under a scheme **approved by the Authority**. [SM 361]
- Bound by the CG on **policy**; independent on technical and administrative matters. The CG may **supersede** it for up to **six months**, appointing a Controller of Insurance. **Insurance Advisory Committee** of up to **twenty-five** members. [SM 362]
- **Annual report** to the CG within **nine months** after each year-end (Dec'25 MCQ = SM MCQ 12; the SM has it only in the exercise).

## M Model answer · indemnity and subrogation (Jun'24 Q7(a)) · 5 marks

(1) **Indemnity**: except life and personal accident, insurance restores the insured to the position before the loss, **no better**; recovery cannot exceed the **actual loss** even within the sum insured (*Vania Silk Mills*). Limits: proof of loss; the sum in the policy; proximate cause; market value. (2) **Subrogation** (a corollary of indemnity): after paying, the insurer acquires the insured's **rights against third parties** who caused the loss, up to the amount paid; the insured must not prejudice those rights, and any excess recovery goes back to the insurer up to its payment. (3) Related: **contribution** among insurers. [SM 351]

**SM SOLVED CASE · AJIT KUMAR WANTS RETAINER FEES FROM 3–4 INSURERS**

**Advice**: (1) commission or reward for procuring insurance may be paid **only to an insurance agent or intermediary**, as the regulations specify (s.40), so he must first **become an agent**; per the SM, a **full-time employee cannot be an agent**. (2) He may act for at most **one life, one general, one health** insurer and one of each mono-line insurer, avoiding **conflicts of interest** (s.42), so "3 or 4" insurers must fit within this. (3) He must comply with the IRDAI's other agent rules. A fixed monthly retainer is not allowed; only regulated commission. [SM 356–357, SM 367]

### The SM's own exercise (SM 363–368)

**MCQs:** 1 life capital **₹100 crore** ★ · 2 (stray BR Act question) **1949** · 3 officer appointed by the CG: **Controller of Insurance** · 4 Government securities **25%** · 5 actuarial valuation every **1 year** · 6 policy unquestionable after **3 years** ★ · 7 regulated by: **none of the above** (it is IRDAI) · 8 IRDA set up in **1999** · 9 **₹100 crore** · 10 chairperson's term **5 years** · 11 Fund: **all of the above** · 12 annual report within **nine months** ★ · 13 no profit from several insurers: **contribution** · 14 an actuary makes a **reasonable forecast** of liabilities · 15 Insurance Laws (Amendment) Act **2015** · 16–17 **all the above** · 18 fire and motor: **both times**. (The SM prints keys for 1–8

only; 9–18 are worked from the SM text.) **True/False:** "indemnity and subrogation" is a principle **T** · the Consumer Protection Act does not apply **F** · an agent can sign all policy documents **F** · health capital ₹300 crore **F** · monitored by IRDA **T**. **Fill-ins:** IRDA · reinsurance · 100 · 3 · indemnified · 1956 · utmost good faith · re-insurance · Central Government · five thousand crore (⚠ now ₹1,000 crore, foreign reinsurers). [SM 363–368]

## R Revision: numbers

| Rule | Number | Rule | Number |
|---|---|---|---|
| Insurance Act in force / LIC from | 1 July 1939 / 1 Sep 1956 | accounts to Authority | 4 copies / 6 months |
| capital: life, general, health / reinsurance | ₹100 cr / ₹200 cr | Govt securities: life / general | 25% + 25% / 25% + 10% |
| FDI (2025 Act) / share-transfer approval above | 100% / 5% | promoter-group investment | ≤ 5% |
| foreign reinsurer NOF (2025 Act) | ₹1,000 cr | solvency: assets over liabilities | ≥ 50% of s.6 capital |
| s.45 policy unquestionable after | 3 years | motor TP non-compliance penalty | ≤ ₹25 cr |
| IRDA: whole-time / part-time members | ≤ 5 / ≤ 4 | chair's term / age; members' age | 5 yrs / 65; 62 |
| supersession / Advisory Committee | ≤ 6 months / ≤ 25 | annual report to CG | 9 months |

# Module 9 · MSME: MSMED Act, 2006 and schemes

P13 · Section B · topics 9.1–9.2

SM pp. 369–384 (16 pages). **32.5 marks in 7 papers.** A **classification MCQ** in 4 papers running (the limits changed on **1 April 2025**); long questions on **delayed payment** (Jun'24, Dec'24) and **schemes** (Jun'23). Section numbers the SM does not print are taken from the Act.

| Paper | What was asked | Marks |
|---|---|---|
| Jun'23 | MCQ: **NSIC** = National Small Industries Corporation (= SM MCQ 1) · Q7(a) **Digital MSME scheme** and **ECLGS** | 2 + 8 |
| Dec'23 | nothing | 0 |
| Jun'24 | MCQ: **medium** limits: ₹50 cr investment / ₹250 cr turnover (the 2020 limits, option A) · Q7(c) **time limit for paying MSMEs** and the consequences of delay | 2 + 4 |
| Dec'24 | Q8(a) **delayed payment**: interest, disallowance, and **disclosure** in the buyer's financial statements | 7 |
| Jun'25 | MCQ: a unit that moves up a category keeps **non-tax benefits for 3 years** (C) · Q7(b)(i) **MSME definition and classification** | 2 + 3.5 |
| Dec'25 | MCQ: the same **3 years** question (B) | 2 |
| Jun'26 | MCQ: investment ₹130 cr, turnover ₹510 cr → **none of the above** (above the 2025 medium limits) | 2 |

**HOW IT IS EXAMINED · DEC'26 PREDICTION**

- **MCQ (x)–(xv): about 50%** chance of a numeric classification question using the **2025 limits**. Learn the table below: test each limit, and the **higher** category wins.
- A long question is unlikely (about 5%); if one comes, it is **delayed payment** (45 days, 3× bank rate, disclosure, disallowance).

**MAP**

1. Definition and 2025 classification ★★★
2. Delayed payment s.15–23 ★★★
3. National Board, Advisory Committee, MSEFC ★
4. Promotion measures, funds, schemes ★★
5. Model answers · SM exercise

## 9.1 Definition and classification · Jun'24, Jun'25, Dec'25, Jun'26 MCQs

The **MSMED Act, 2006** gave the first legal framework for the concept of an "**enterprise**" covering both **manufacturing and services**, a statutory consultative mechanism, dedicated funds, credit policies, **procurement preference**, remedies for **delayed payments**, and a scheme to ease **closure**. Promotion is primarily the **State Governments'** job; the Centre supplements it. The sector has **3.6 cr** units and **8 cr** employees (second only to agriculture): **45%** of industrial output, **40%** of exports, **37%** of GDP. [SM 371]

| Composite criteria | Micro | Small | Medium |
|---|---|---|---|
| SM (from 1 July 2020): investment / turnover | ≤ ₹1 cr / ≤ ₹5 cr | ≤ ₹10 cr / ≤ ₹50 cr | ≤ ₹50 cr / ≤ ₹250 cr [SM 371] |
| **From 1 April 2025** (Jun'26 supplementary) | **≤ ₹2.5 cr / ≤ ₹10 cr** | **≤ ₹25 cr / ≤ ₹100 cr** | **≤ ₹125 cr / ≤ ₹500 cr** [Supp Jun'26] |

**HOW TO CLASSIFY**

- **Both** limits must be met for a category; if **either** is exceeded, the unit moves to the next category. (The Act's rule, implied by "composite".)
- **Investment** in plant, machinery or equipment is linked to the **previous year's ITR** (else self-declaration); tangible assets **other than land and furniture and fittings** (SM MCQ 3). [SM 372]
- **Turnover excludes exports** (SM MCQ 4) and is linked to income-tax and GST returns. [SM 372]
- A unit that moves to a higher category, or out of MSME, keeps its **non-tax benefits for the next 3 years** (Jun'25, Dec'25 MCQ). [SM 372]

**WORKED MCQs (2025 LIMITS)**

- Jun'26: ₹130 cr / ₹510 cr → both exceed medium → **not an MSME** (D).
- SM MCQ 2: ₹55 cr / ₹300 cr → key (d) "none" under the **2020** limits; under the **2025** limits it is **medium**. Read the question's date.
- ₹3 cr investment / ₹8 cr turnover → investment exceeds micro → **small**.
- The supplementary also says existing units kept their status until **31 March 2025** (reverse graduation).

## 9.2 Delayed payment to micro and small enterprises · Jun'24 Q7(c), Dec'24 Q8(a)

**THE SM'S RULE (s.15–16, 22)**

- **Appointed day**: the day after **15 days** from the buyer's (deemed) receipt of goods or services. **Day of acceptance**: the day of actual delivery or performance, or, if the buyer objects in writing **within 15 days**, the day the supplier removes the objection. **Deemed acceptance**: no written objection within 15 days. [SM 374]
- Payment may not exceed **45 days** from the day of acceptance or deemed acceptance. Otherwise the buyer pays **compound interest with monthly rests**, from the appointed day (or the agreed date), at **three times the bank rate** notified by the RBI. [SM 377]
- A buyer whose accounts are audited discloses the **principal and interest unpaid** to any supplier at the end of each year; this **interest is not deductible** from income. [SM 377]
- Companies with dues to MSEs **outstanding 45 days or more** file a **half-yearly return with the MCA** (2 Nov 2018). Suppliers may complain on the **MSME Samadhan** portal. [SM 379]
- **Disputes (s.18)**: a reference to the **Micro and Small Enterprises Facilitation Council**, which conciliates (itself or through an ADR centre) and, if that fails, **arbitrates**; it covers a supplier in its jurisdiction and a buyer **anywhere in India**; decided within **90 days**. [SM 376]

**⚠ WHAT DEC'24 Q8(a) ALSO NEEDED (NOT IN THE SM)**

- **s.15**: any written agreement on payment terms may not exceed **45 days**; with no agreement, pay before the **appointed day**.
- **s.22 disclosure** in the buyer's annual accounts: (i) **principal and interest unpaid** at year-end, shown separately; (ii) **interest paid under s.16**, with the amounts paid **after the appointed day**; (iii) interest **due and payable for the period of delay** (paid late but without interest); (iv) interest **accrued and remaining unpaid** at year-end; (v) **further interest** remaining due in later years until it is actually paid, for disallowance under s.23. Schedule III also asks for MSME dues to be shown separately.
- **s.23**: interest payable under s.16 is **not deductible** under the Income-tax Act.
- **Income-tax s.43B(h)** (from FY 2023-24): a payment due to a micro or small enterprise is deductible **only in the year it is actually paid** if it is paid after the s.15 time limit.
- **Registration**: the SM's "memorandum" was replaced from 1 July 2020 by online, free **Udyam Registration** on self-declaration.

## 9.2 Bodies, promotion measures and funds · SM short essay 2

- **s.9 promotion**: the CG may notify programmes for competitiveness, **skills**, management, **technology upgradation**, marketing, infrastructure, **cluster development**, backward and forward linkages; **s.10** smooth credit; **s.11 procurement preference** (notified 23 March 2012). [SM 373, SM 377, SM 379]
- **Ministry of MSME**: the apex policy body (SM T/F 1: not the Ministry of Commerce). Formed from the SSI and Agro and Rural Industries ministries (created October 1999). [SM 373]
- **National Board (s.3)**, HQ Delhi: the MSME **Cabinet Minister** chairs; the MoS is vice-chair; **six** State ministers; **three** MPs (two Lok Sabha, one Rajya Sabha); secretaries; heads of NABARD, SIDBI, IBA; an RBI Executive Director; **20** association members (at least 3 women's, 3 micro); 3 eminent persons (one a woman); 2 trade-union members. Meets at least once every **3 months**. [SM 374–375]
- **Board's functions**: examine factors affecting MSME growth and review Government policies; make **recommendations**; **advise the CG on use of the Fund**. [SM 375]
- **Advisory Committee (s.7)**: the MSME Secretary chairs; up to **five** CG officers; up to **three** State representatives; one representative each of MSME associations; the Board's Member-Secretary. The CG must take its recommendations before classifying enterprises. [SM 376–377]
- **Facilitation Councils (s.20–21)** set up by the State Government: **three to five** members: the Director of Industries, MSE association office-bearers, bank representatives, experts. [SM 377–378]
- **Funds (s.12–14)**: notified funds, credited with CG grants, used **exclusively for MSMEs**. [SM 377]
- **Revival framework** (27 May 2015): banks form committees to restructure stressed MSME loans. Single-window registration via the Champions control room and DICs. [SM 379]

| Scheme or body | What the SM says |
|---|---|
| **NSIC** (1955) | **National Small Industries Corporation**: promotes micro and small enterprises on a commercial basis: raw materials, marketing, **credit rating**, technology, management [SM 380] |
| **Digital MSME** ★ | promotes **ICT** in MSMEs' production and business: **ERP**, accounting, manufacturing design, **GST compliance**; awareness, e-platforms, digital literacy, training and **digital marketing** [SM 380] |
| **ECLGS** ★ | COVID-19 scheme: **100% guarantee** to banks and NBFCs for emergency credit (additional term loan or working capital); extended to **31 March 2022**; interest capped at **9.25%** (banks) and **14%** (NBFCs); tenure **4 years**; principal moratorium **12 months** [SM 380] |

| | |
|---|---|
| **SIDBI Secured Business Loan** | term loan up to **₹10 crore**, repayment up to **10 years** including moratorium; foreign-currency assistance [SM 380] |
| **PMEGP** | credit-linked subsidy for **employment** through new micro-enterprises, rural and urban [SM 381] |
| **Others** | reservation and easier licensing; International Cooperation Scheme (trade delegations); NIESBUD training |
| **COVID package** | ₹3 lakh crore emergency working capital (**20%** of credit outstanding on 29 Feb 2020); **₹20,000 crore** subordinate debt for **2,00,000** stressed MSMEs, with ₹4,000 crore to CGTMSE; promoters get **15%** of their stake, up to **₹75 lakh**; Fund of Funds of **₹10,000 crore** to mobilise **₹50,000 crore** of equity [SM 381] |

## M Model answers

**MODEL ANSWER 1 · DELAYED PAYMENT: TIME LIMIT, INTEREST, DISALLOWANCE, DISCLOSURE (DEC'24 Q8(a), JUN'24 Q7(c)) · 7 MARKS**

(1) **Time limit (s.15)**: by the agreed date, never more than **45 days** from acceptance or deemed acceptance; with no agreement, before the **appointed day** (15 days). Define acceptance and deemed acceptance. (2) **Interest (s.16)**: **compound with monthly rests** at **three times the RBI bank rate**, from the appointed day or agreed date. (3) **Disallowance**: that interest is **not deductible** (s.23); and under s.43B(h) a late payment itself is deductible only when paid. (4) **Disclosure (s.22)**: the five items in the ⚠ box. (5) **Recovery**: reference to the **MSEFC** (conciliation, then arbitration, within 90 days); half-yearly MCA return; MSME Samadhan. [SM 374, SM 376–377, SM 379]

**MODEL ANSWER 2 · SM SOLVED CASE: BALARAM'S RUBBER-SPARES FIRM**

**Facts as printed:** a proprietorship making rubber spares; turnover ₹342 crore; plant and machinery about ₹93 lakh; GST-registered, not DIC-registered. **SM answer:** (i) **micro** enterprise; (ii) registration is **not compulsory**, but benefits need it; (iii) register with the **District Industries Centre**; (iv) benefits: **loans, moratorium on repayment, tax holidays, price preference** in Government purchases. [SM 383–384]

⚠ The SM's category is wrong for the figures it prints: with turnover of ₹342 crore the unit exceeds the micro turnover limit, so it is **not micro** (2020 limits: above medium too, so not an MSME; 2025 limits: **medium**). The SM probably meant ₹3.42 crore. Today registration is online on the **Udyam** portal. In the exam, apply the limits to the figures given.

### The SM's own exercise for MSME (SM 382–384)

**MCQs:** 1 NSIC = **National Small Industries Corporation** ★ · 2 ₹55 cr / ₹300 cr = **none** (2020 limits; medium under 2025) ⚠ · 3 excluded from investment: **land and furniture and fittings** · 4 excluded from turnover: **exports**. **True/False:** apex body is the Ministry of Industry and Commerce **F** · basis is investment and turnover **T** · a CG licence is needed to start an MSME **F** · delayed payments are reported in companies' annual reports **T** · banks give subordinate loans 15% above limits **T** (key; the SM text says 15% of the promoter's stake). **Fill-ins:** micro threshold **₹1 crore** (now ₹2.5 crore) · interest if delayed beyond **45** days · **National Small Industries Corporation** · **₹20,000 crore** subordinate debt · SIDBI = **Small Industries Development Bank** of India · **15**% · PMEGP relates to **employment** · ECLGS = **Emergency Credit Line Guarantee Scheme** · SBL up to **₹10 crore**. [SM 382–384]

## R Revision: numbers

| Rule | Number | Rule | Number |
|---|---|---|---|
| micro / small / medium (2025): investment | ₹2.5 / 25 / 125 cr | objection to goods or services within | 15 days |
| micro / small / medium (2025): turnover | ₹10 / 100 / 500 cr | maximum credit period | 45 days |
| non-tax benefits after moving up | 3 years | interest on delay | 3 × bank rate, monthly compound |
| National Board meets at least every | 3 months | MSEFC decides within | 90 days |
| MSEFC members | 3 to 5 | ECLGS rate cap banks / NBFCs | 9.25% / 14% |
| Board: State ministers / MPs / associations | 6 / 3 / 20 | ECLGS tenure / moratorium | 4 yrs / 12 months |

# Module 10 · Cyber Security and Data Privacy

P13 · Section B · topics 10.1–10.3

SM pp. 385–400 (16 pages). **53.5 marks in 7 papers.** A 7-mark long question in 6 of 7 papers (usually Q6(b)); **business intelligence** alone has had three. An MCQ in every paper except Dec'25. Section numbers the SM does not print are taken from the Act.

| Paper | What was asked | Marks |
|---|---|---|
| Jun'23 | MCQ: **trespass** (= SM MCQ 10) · Q7(b)(ii) list **5 cyber crimes under the IPC** and special laws | 2 + 3 |
| Dec'23 | MCQ: e-governance PPP for grievances, land records and services = **Lokvani (UP)**, not in the SM · Q6(b) **how the BI process works** | 2 + 7 |
| Jun'24 | MCQ: **embedded BI** (= SM fill-in 7) · Q6(a) **business intelligence**: meaning and benefits | 2 + 7 |
| Dec'24 | MCQ: Cyber Appellate Tribunal → **High Court** (= SM MCQ 6) · Q3(b) **data protection** under the IT Act and the law in India today | 2 + 7 |
| Jun'25 | MCQ: **not an IT Act crime**: threatening e-mail (= SM MCQ 8) · Q5(b)(i) **cyber crimes against persons** | 2 + 3.5 |
| Dec'25 | Q6(b) **how the BI process works** (repeat of Dec'23) | 7 |
| Jun'26 | MCQ: offences on **unauthorised access** · Q6(b) **identity theft and cheating by personation**; adjudication and penalties (not in the SM) | 2 + 7 |

**HOW IT IS EXAMINED · DEC'26 PREDICTION**

- **Q6(b), 7 marks**: (1) **BI process + benefits** (asked 3 times, in the PTP; about 45%); (2) **data protection / SPDI Rules** (25%); (3) **s.43 compensation** (ICMAI MQP Q6(b), not in the SM; see the ⚠ box); (4) cyber crimes (20%).
- MCQs come from the SM exercise; the Dec'26 supplementary adds **synthetically generated information** (MCQ material).

**MAP**

1. IT Act: objects, CCA, offences, appeals ★★
2. Data protection: s.43A, s.72A, SPDI Rules ★★★
3. ⚠ DPDP Act 2023; s.43, 66C, 66D ★★
4. Business intelligence: process, benefits, tools ★★★
5. Cyber crimes: persons, property, Government ★★
6. Model answers · SM exercise

## 10.1 Information Technology Act, 2000 · Dec'24 MCQ

**OBJECTS · RECORDS · CCA**

- **Objects**: (i) **legal recognition of electronic transactions** through digital signatures, including electronic publication of rules and gazette notifications; (ii) **electronic filing** and retention of documents with Government (the public cannot be forced to use only the electronic mode); (iii) consequential amendments to other Acts; (iv) set up the **licensing, monitoring and certifying authority**. [SM 387]
- **Dispatch** occurs when a record enters a resource outside the originator's control; **receipt** when it enters the addressee's designated computer resource (or when retrieved, if none is designated); place of business is the place of dispatch and receipt. [SM 387]
- **Controller of Certifying Authorities** (CCA), appointed by the CG: recognises, **licenses**, regulates and supervises **certifying authorities**, which **issue digital signature certificates** (SM MCQ 1 and a fill-in). The CG/Controller may intercept information for security and declare **protected systems**. [SM 387]

**OFFENCES · DISPUTES**

- Applies to any offence by anyone, anywhere, if it involves a **computer, system or network located in India**. [SM 387]
- Offences: (a) **tampering with computer source documents**; (b) **hacking** (destroying, deleting or altering data with intent to cause damage); (c) **misrepresentation** to the Controller or a CA; (d) **breach of confidentiality and privacy**; (e) **publishing false digital signature certificates**. [SM 387]
- **Disputes**: the CG appoints **adjudicating officers** with IT and legal knowledge. Appeal against the Controller or an adjudicating officer to the **Cyber Appellate Tribunal within 45 days**; its decision may be appealed to the **High Court within 60 days** (the SM prints "6o") (Dec'24 MCQ = SM MCQ 6). **Civil courts have no jurisdiction.** [SM 388] ⚠ Since 2017 the Cyber Appellate Tribunal's work is done by the TDSAT.

## 10.1.2 Data protection: s.43A, s.72A and the SPDI Rules, 2011 · Dec'24 Q3(b)

**WHAT IT IS · THE LAW (SM)**

SM WORDS **Data protection** refers to the set of privacy laws, policies and procedures that aim to **minimise intrusion into one's privacy** caused by the **collection, storage and dissemination of personal data**. Personal data is information

**SPDI RULES, 2011 (NOTIFIED 11 APRIL 2011) · SM ESSAY 3, 4**

1. Apply only to **bodies corporate and persons located in India** (SM MCQ 7). [SM 388]
2. **Rule 3**: sensitive personal data includes **passwords**, **card details**, **biometrics** (DNA, fingerprints, voice patterns),

relating to a person who can be **identified** from it, whether collected by Government or a private body. [SM 388]

- The IT Act came into force on **17 Oct 2000** without data-protection provisions; the **2008 Amendment** (in force **27 Oct 2009**) inserted **s.43A**, and the CG notified the **2011 Rules**. Privacy became a **fundamental right** on **24 Aug 2017** (an SM fill-in). [SM 388]
- **s.43A**: a body corporate that holds **sensitive personal data** and is **negligent in maintaining reasonable security**, causing wrongful loss or gain, is **liable to pay damages** to those affected. [SM 388]
- **s.72A**: disclosing information **in breach of a lawful contract**: imprisonment up to **three years**, or fine up to **five lakh rupees**, or both. [SM 388]

physical, physiological and **mental health**. Information freely available in the public domain is not sensitive. [SM 388]

3. **Rule 4**: a **privacy policy**, published on the website: what is collected, why, and the security practices. [SM 389]
4. **Rule 5**, duties when collecting: **consent**; collect only for a **lawful, necessary purpose**, use only for it and do not keep it longer than needed; tell the person the purpose, recipients and who holds it; let them **review and correct** it; keep it **secure**; appoint a **Grievance Officer** named on the website. [SM 389]
5. **Prior permission** of the provider before disclosing to a **third party**. [SM 389]
6. **Rule 8**: reasonable security practices, e.g. **IS/ISO/IEC 27001**; an **audit at least once a year** or on a significant upgrade. [SM 389]

**⚠ "THE LAW AS PREVALENT IN INDIA TODAY": DIGITAL PERSONAL DATA PROTECTION ACT, 2023 (NOT IN SM)**

The SM says India has no separate data-protection law; that is out of date. The **DPDP Act, 2023** (assent 11 Aug 2023) applies to **digital personal data** processed in India, and abroad when offering goods or services to people in India. Personal data may be processed only for a lawful purpose with the person's **consent** (after a notice), or for certain **legitimate uses**. **Data fiduciaries** must keep data accurate, take **security safeguards**, report **breaches**, and **erase** data once the purpose is served. **Data principals** have rights to **access, correction and erasure**, grievance redressal and to nominate. A child's data needs **verifiable parental consent**. **Significant data fiduciaries** appoint a DPO and conduct audits. The **Data Protection Board of India** adjudicates; penalties go up to **₹250 crore**. The DPDP Rules were notified in Nov 2025, with most duties applying after 18 months; s.43A and the SPDI Rules are to be replaced by it. In the answer: **write the SM part first**, then this paragraph.

## ⚠ IT Act sections the SM leaves out · ICMAI MQP Q6(b), Jun'26 Q6(b)

**s.43 · ACTS THAT ATTRACT COMPENSATION (MQP)**

If any person, **without permission** of the owner or person in charge of a computer, system or network: (a) **accesses** it; (b) **downloads or copies** data; (c) introduces a **virus**; (d) **damages** it or its data; (e) **disrupts** it; (f) **denies access** to an authorised person; (g) **helps** another to access it in breach of the Act; (h) **charges** services used by one person to another's account; (i) **destroys, deletes or alters** information or reduces its value; (j) **steals or alters source code**: he is liable to pay **damages by way of compensation** to the person affected. Doing any of these **dishonestly or fraudulently** is the offence under **s.66** (up to 3 years or fine up to ₹5 lakh, or both).

**s.66C, 66D · ADJUDICATION (JUN'26 Q6(b))**

- **s.66C identity theft**: fraudulently or dishonestly using another person's **electronic signature, password or other unique identification**: imprisonment up to **3 years** and fine up to **₹1 lakh**.
- **s.66D cheating by personation** using a computer resource or communication device: imprisonment up to **3 years** and fine up to **₹1 lakh**.
- **Adjudication (s.46)**: the CG appoints an **adjudicating officer** (a Government officer of at least Director rank) who holds an inquiry after a reasonable opportunity of hearing, for claims up to **₹5 crore**; above that, the **civil court**. Factors (s.47): unfair gain, loss caused, repetitive nature. Appeals: Tribunal in **45 days** → High Court in **60 days** (as in the SM).
- Others: **s.65** tampering with source code: 3 years or ₹2 lakh; **s.67** obscene material: 3 years and ₹5 lakh (first conviction); **s.72** breach of confidentiality by an official: 2 years or ₹1 lakh.

**SUPPLEMENTARIES**

**Dec'26: synthetically generated information (SGI)**: IT (Intermediary Guidelines and Digital Media Ethics Code) Rules amended (notified **10 Feb 2026**, effective **20 Feb 2026**). SGI = audio, visual or audio-visual content **generated or altered by technology so that it appears authentic** or represents a real person, event or fact. Intermediaries must **label** it clearly, embed **technical or provenance information** (prescribed intermediaries), and act to **remove or restrict unlawful SGI**. [Supp Dec'26 p.9] **Jun'26:** the RBI required scheduled banks to move to the **".bank.in"** internet domain by **31 Oct 2025**. [Supp Jun'26]

## 10.2 Business intelligence · Dec'23 Q6(b), Jun'24 Q6(a), Dec'25 Q6(b), PTP Q6(b)

SM WORDS **Business Intelligence (BI)** is a **technology-driven process for analyzing data and delivering actionable information** that helps executives, managers and workers make **informed business decisions**. Organisations **collect** data from internal systems and external sources, **prepare** it, **run queries**, and create **visualizations, dashboards and reports** for operational decisions and strategic planning. The goal: **better decisions** that increase revenue, improve efficiency and give a **competitive advantage**. [SM 390]

### HOW THE BI PROCESS WORKS (ASKED TWICE)

- **Architecture**: data is stored in an enterprise **data warehouse** or smaller departmental **data marts**; it may be **historical or real-time**, so BI supports strategic and tactical decisions. [SM 390]
- Raw data from different sources is **integrated, consolidated and cleansed** with data-integration and data-quality tools so that analysis is accurate and consistent. [SM 390]

**(a) Data preparation** organise and model data sets → **(b) Analytical querying** of the prepared data → **(c) Distribution** of KPIs and findings → **(d) Use** to drive decisions

- **Self-service BI**: business users now query data and build dashboards themselves. **Advanced analytics** (data mining, predictive analytics, text mining, statistics, big data; e.g. what-if modelling) is usually done by data scientists. [SM 390]
- **Why it matters**: without BI, decisions rest on experience, intuition and "gut feelings", which risk errors. [SM 391]

### BENEFITS (JUN'24)

Managers **monitor performance continuously**; customer analysis improves marketing, sales and service; **supply-chain bottlenecks** are found early; HR tracks productivity and labour cost. Key benefits: [SM 391]

1. **faster, better decision-making**
2. **optimised internal processes**
3. higher **operational efficiency and productivity**
4. spotting **business problems**
5. identifying **emerging business and market trends**
6. stronger **business strategies**
7. higher **sales and new revenues**
8. a **competitive edge** over rivals

Also: tracking projects; **competitive intelligence**; IT teams analyse their own operations (SM MCQ 5: all of the above). [SM 391]

| BI tool | Meaning (SM) |
|---|---|
| **Ad hoc analysis** | writing and running queries on a specific business issue, on a casual or temporary basis [SM 391] |
| **OLAP** (online analytical processing) | analysis along **multiple dimensions**; complex queries and calculations |
| **Mobile BI** | dashboards on smartphones and tablets, showing two or three visualisations and KPIs |
| **Real-time BI** · **operational intelligence** | data analysed as it is created (credit scoring, stock trading, targeted offers) · real-time analytics for frontline workers [SM 391–392] |
| **Open source BI (OSBI)** | a free community edition and a paid commercial version with vendor support (SM MCQ 4) |
| **Embedded BI ★** | puts BI and data-visualisation functions **directly into business applications** (Jun'24 MCQ = SM fill-in 7) |
| **Collaborative BI** | BI plus collaboration tools: users annotate and share analysis |
| **Location intelligence** | geospatial data on maps: store sites, location-based marketing, logistics [SM 392] |

**Platforms**: visualisation software; dashboards, reports and scorecards; **data storytelling**; usage monitoring and security. **Uses**: performance monitoring, decisions and planning, process improvement, operational information, trends and patterns. By industry: banks and insurers (risk analysis, cross-selling), retail (campaigns, inventory), manufacturing (plant operations), airlines and hotels (capacity, pricing), healthcare, education. **Trends**: BI teams (architects, developers, analysts) and **Agile BI** replacing waterfall development. [SM 392–393]

## 10.3 Cyber crime: meaning, types, laws · Jun'23 Q7(b)(ii), Jun'25 Q5(b)(i)

SM WORDS **Cybercrime** is criminal activity in which **computers or computer networks are a tool, a target, or a place** of criminal activity: phishing, credit-card fraud, illegal downloading, industrial espionage, child pornography, scams, cyber terrorism, viruses. It has **no geographical boundaries** and the criminals are unknown. [SM 394]

### A. AGAINST PERSONS (JUN'25 Q5(b)(i))

- **Cyber-stalking**: creating fear of physical threat through internet, e-mail, phones, texts, webcams or websites. [SM 394]
- **Obscenity**: indecent exposure, pornography (especially child pornography), hosting such sites.
- **Defamation**: lowering a person's dignity, e.g. hacking his mail and sending vulgar mails (SM fill-in 6).
- **Hacking**: unauthorised control or access over a computer system. **Cracking**: breaking in and tampering with confidential data. [SM 394–395]
- **Spoofing**: e-mail or SMS that misrepresents its origin. **Carding**: false ATM, debit or credit cards. **Fraud**: stealing

### B. AGAINST PROPERTY · C. AGAINST GOVERNMENT

- **Property**: IPR violation (software piracy, copyright, trade marks); **squatting** (two persons claiming the same domain name); **vandalism** (destroying data or disrupting a network); hacking; **viruses and worms**; **trespass**: accessing a computer without authority but **not disturbing, altering or damaging** it, e.g. over wireless internet (Jun'23 MCQ = SM MCQ 10). [SM 395]
- **Government**: **cyber terrorism** (DDoS, hate sites, attacks on sensitive networks); **warfare** (politically motivated hacking and spying); **piracy**; **unauthorised information**. [SM 395–396]

passwords and data with a guilty mind. **Threat**: threatening life through e-mail, videos or phones. [SM 395]

| Under the IT Act (SM ESSAY 2; SM MCQ 8) | Under the IPC (Jun'23 Q7(b)(ii): any 5) and special laws |
|---|---|
| (i) tampering with computer source documents: **s.65**<br>(ii) hacking, data alteration: **s.66**<br>(iii) publishing obscene information: **s.67**<br>(iv) unauthorised access to a protected system: **s.70**<br>(v) breach of confidentiality and privacy: **s.72**<br>(vi) publishing false digital signature certificates: **s.73**<br>[SM 396] | (i) threatening e-mail: **s.503** · (ii) defamatory e-mail: **s.499** · (iii) forgery of electronic records: **s.463** · (iv) bogus websites, cyber frauds: **s.420** · (v) e-mail spoofing: **s.463** · (vi) web-jacking: **s.383** · (vii) e-mail abuse: **s.500**. **Special Acts**: online sale of drugs (NDPS Act); online sale of arms (Arms Act). [SM 396]<br>⚠ The IPC was replaced by the Bharatiya Nyaya Sanhita from 1 July 2024 (e.g. cheating 420 → BNS 318; forgery 463 → 336; intimidation 503 → 351; defamation 499 → 356; extortion 383 → 308). Quote the SM's IPC numbers and add "now BNS". |

*Jun'25 MCQ: "threatening messages by e-mail" is an IPC crime, not an IT Act one (A). Jun'26 MCQ: the SM groups s.65, 66 and 72 together under "unauthorised information", which points to (D) all of the above.*

## M Model answers

**MODEL ANSWER 1 · HOW BI WORKS AND ITS BENEFITS (DEC'23, DEC'25 Q6(b); JUN'24 Q6(a); PTP) · 7 MARKS**

(1) **Definition** in the SM's words (above). (2) **Architecture**: data warehouse and data marts; historical and real-time data; integrate, consolidate and cleanse. (3) **Four steps**: data preparation → analytical querying → distribution of KPIs → use in decisions. (4) **Self-service BI** and **advanced analytics**. (5) **Benefits**: the eight points. (6) A line on **tools** (OLAP, embedded, mobile, real-time). For "BI in the context of cyber security" (Jun'24): add that BI needs **secure, accurate data**; data-protection duties (SPDI Rules) apply to the data it uses. [SM 390–392]

**MODEL ANSWER 2 · DATA PROTECTION UNDER THE IT ACT AND IN INDIA TODAY (DEC'24 Q3(b)) · 7 MARKS**

(1) Meaning of data protection (SM words). (2) **Background**: IT Act 2000; 2008 Amendment inserted **s.43A**; SPDI Rules 2011; privacy a fundamental right (24 Aug 2017). (3) **s.43A** damages and **s.72A** punishment (3 years / ₹5 lakh). (4) **SPDI Rules**: who they apply to; sensitive data (Rule 3); privacy policy (Rule 4); collection duties (Rule 5); third-party disclosure; security and annual audit (Rule 8). (5) **Today**: the DPDP Act 2023 (⚠ box). [SM 388–389]

### The SM's own exercise for Cyber and Data (SM 397–400)

| | | | |
|---|---|---|---|
| 1 CAs licensed by | **Controller of Certifying Authorities** | 6 Cyber Appellate Tribunal → ★ | **High Court** |
| 2 not an IT Act offence | **making a faulty contract** | 7 SPDI Rules apply to | **bodies corporate and persons in India** |
| 3 SPDI Rules notified in | **2011** | 8 not an IT Act crime ★ | **threatening e-mail** |
| 4 OSBI | **open source business intelligence** | 9 not a cyber offence to the public | **data alteration** |
| 5 BI benefits | **all of the above** | 10 access without altering ★ | **trespass** |

**True/False:** tampering with source documents is not an offence **F** · the CCA issues digital signature certificates **F** (certifying authorities do) · appeal to the Cyber Appellate Tribunal **T** · unauthorised access without damage = trespass, an offence **T** · BI facilitates analytical querying **T**. **Fill-ins:** CCA = **Controller of Certifying Authorities** · appeal from the adjudicating officer to the **Cyber Appellate Tribunal** · rules preserving privacy = **data protection** · KPI = **key performance indicators** · OLAP = **online analytical processing** · **defamation** · **embedded BI** ★ · certificates issued by the **certifying authority** · SPDI Rules **2011** · privacy a fundamental right in **2017**.

## R Revision: numbers

| Rule | Number | Rule | Number |
|---|---|---|---|
| IT Act in force / 2008 amendment in force | 17 Oct 2000 / 27 Oct 2009 | appeal to Tribunal / High Court | 45 / 60 days |
| SPDI Rules notified | 11 Apr 2011 | s.72A | 3 yrs or ₹5 lakh |
| privacy a fundamental right | 24 Aug 2017 | security audit (Rule 8) | at least once a year |
| s.66C / s.66D (Act) | 3 yrs + ₹1 lakh each | adjudicating officer up to (Act) | ₹5 crore |
| SGI rules notified / effective | 10 / 20 Feb 2026 | DPDP penalty up to (Act) | ₹250 crore |

# Module 11 · Prevention of Money Laundering Act, 2002 P13 · Section B · topics 11.1–11.2

SM pp. 401–410. **26 marks in 7 papers.** Long questions in 4 of the first 5 papers (process, schedules, key features), then MCQs only. The ICMAI MQP has a fresh long one: **the offence (s.3) and its punishment (s.4)**.

| Paper | What was asked | Marks |
|---|---|---|
| Jun'23 | Q7(b)(i) the **process of money laundering** | 5 |
| Dec'23 | nothing | 0 |
| Jun'24 | Q6(c) the **process of money laundering** again | 3 |
| Dec'24 | MCQ: PMLA cases go to **special designated courts** (= SM MCQ 7) · Q7(b) **offences in the schedules** (Parts A, B, C) | 2 + 7 |
| Jun'25 | Q8(b) **key features** of the PMLA: any seven | 7 |
| Dec'25 | MCQ: every scheduled offence is a **predicate offence** (= SM fill-in 2) | 2 |
| Jun'26 | nothing | 0 |

**HOW IT IS EXAMINED · DEC'26 PREDICTION**

- All past questions are **SM paragraphs**. Two blank papers in a row, so a long question may return: **s.3 offence + s.4 punishment** (MQP Q8(a)), or key features again.
- MCQ: about 20%: placement, predicate offence, special courts, ₹10 lakh, 10 days, 5 years.

**MAP**

1. Meaning, history, objects ★★
2. Process: placement, layering, integration ★★★
3. Offence, schedules, punishment ★★★
4. ED, FIU-IND, AA, Tribunal, Special Courts ★★
5. Reporting entities, STRs, Record Rules 2005 ★★

## 11.1 Meaning, history and objects · Jun'25 Q8(b)

- **Money laundering** is the processing of criminal proceeds (from arms sales, smuggling, drug trafficking, embezzlement, insider trading, bribery, computer fraud) **to disguise their illegal origin**: converting "**dirty money**" so that it appears **legitimate**. [SM 403]
- A global problem: India is a member of the **Financial Action Task Force** and the **Asia Pacific Group** on money laundering. [SM 403]
- Enacted in **January 2003**; in force with its Rules from **1 July 2005**; extends to the whole of India; amended in **2009** (from 1 June 2009) and **2012** (from 15 Feb 2013). It meets the obligations of the UN General Assembly's **Political Declaration and Global Programme of Action**. [SM 403]
- Structure: **ten chapters, 75 sections**, one Schedule; Ch. II (s.3–4) offence and punishment; Ch. III (s.5–11) attachment, adjudication, confiscation; Ch. IV (s.12–15) obligations of banks, FIs and intermediaries; Ch. V (s.16–24) summons, search and seizure. [SM 403]

**OBJECTS**

a. to **prevent and control** money laundering;
b. to **confiscate and seize** property obtained from laundered money;
c. to deal with any other issue connected with money laundering in India.

[SM 404]

**THE PROCESS: JUN'23, JUN'24**

**(a) Placement** illegal funds enter the financial system: cash split into small deposits, or bought instruments (cheques, drafts) deposited elsewhere →→ **(b) Layering** a series of conversions and movements through many accounts, often abroad in non-cooperating jurisdictions, to hide the origin →→ **(c) Integration** funds rejoin the legitimate economy, mixed with legal income: real estate, businesses, luxury assets

[SM 404]

*SM MCQ 6: introducing illegal funds into the financial system = **placement**.*

## s.3–4 Offence, scheduled offences, punishment · Dec'24 Q7(b), Dec'25 MCQ, MQP Q8(a)

**THE OFFENCE (s.3) · THE MQP ANSWER**

SM WORDS Whosoever **directly or indirectly attempts to indulge** or **knowingly assists** or **knowingly is a party** or is

**THE SCHEDULE (DEC'24 Q7(b))**

- **Part A** (**28 paragraphs**): offences under the **IPC**, **NDPS Act**, Explosive Substances Act 1908, **Unlawful Activities**

**actually involved** in any process or activity connected with the **proceeds of crime**, including its **concealment, possession, acquisition or use**, or **projecting or claiming it as untainted property**, shall be guilty of the offence of money-laundering. [SM 404]

SM WORDS **Punishment (s.4)**: **rigorous imprisonment** for not less than **three years**, which may extend to **seven years**, **and fine**. Where the proceeds relate to an offence in **paragraph 2 of Part A** of the Schedule (the NDPS Act), the maximum is **ten years**. Property derived from proceeds of crime may be **attached and confiscated**. [SM 405]

Add for depth (from the Act): "proceeds of crime" = property derived from criminal activity relating to a scheduled offence; the 2019 Explanation makes the offence a **continuing activity** and covers each of the listed acts on its own; upheld in *Vijay Madanlal Choudhary v. UoI* (SC, 2022).

**(Prevention) Act 1967**, Arms Act 1959, Wild Life (Protection) Act 1972, Immoral Traffic (Prevention) Act 1956, **Prevention of Corruption Act 1988**, Explosives Act 1884, Antiquities and Art Treasures Act 1972, **SEBI Act 1992**, **Customs Act 1962**, etc. [SM 404–405]

- **Part B**: offences where the total value involved is **₹1 crore or more** (SM MCQ 3). [SM 405] Since 2015 Part B holds the Customs Act s.132 false-declaration offence.
- **Part C**: **trans-border crimes**, a vital step against laundering across borders. [SM 405]
- SM WORDS **Every scheduled offence is a predicate offence.** Its occurrence is a **pre-requisite** for starting an investigation into money laundering (Dec'25 MCQ: (D)). [SM 405]

## 11.1 Authorities, investigation, courts · Dec'24 MCQ

| Authority | Role (SM) |
|---|---|
| **Directorate of Enforcement** (ED) | Department of Revenue, Ministry of Finance: **investigates and prosecutes** money-laundering cases and **attaches property**; also enforces **FEMA** (SM fill-in 1) [SM 404–406] |
| **FIU-IND** | set up in **November 2004**, headed by a Director of Joint Secretary rank: the central agency that **receives, processes, analyses and disseminates** information on suspect transactions to enforcement agencies and foreign FIUs; receives **CTRs and STRs** under s.12; may **fine** reporting entities for non-compliance; reports to the **Economic Intelligence Council** headed by the Finance Minister [SM 404–406] |
| **Adjudicating Authority** (s.6) | appointed by the CG; if property is involved in money laundering, it **confirms the attachment** (s.5) or the retention of seized property, or orders **confiscation** [SM 405–406] |
| **Appellate Tribunal** (s.25) | a Chairperson and **two** members (the ATFP's chairman and a member hold additional charge); hears appeals against the Adjudicating Authority, the Director of FIU-IND and other authorities [SM 405–406] |
| **Special Courts ★** | the CG, **in consultation with the Chief Justice** of the High Court, designates **Courts of Session** as Special Courts; they try the s.4 offence and any connected **scheduled offence**, for the area where it was committed (Dec'24 MCQ = SM MCQ 7; SM short essay 2) [SM 405, SM 407] |
| **International** | **reciprocal arrangements** and bilateral agreements with foreign states to enforce the Act and exchange information [SM 405] |

**JUN'26 SUPPLEMENTARY**

**I4C**: on **25 April 2025** the Indian Cyber Crime Co-ordination Centre was notified as a "financial institution" under s.66, so it can exchange financial intelligence with the **ED** (online money trails). **2025 framework**: **risk-based KYC** (enhanced due diligence for high-risk customers, simplified updating for low-risk ones, more digital identity checks); continuous monitoring; updating **beneficial ownership**; **STRs through upgraded FIU utilities**; automated transaction monitoring. [Supp Jun'26 p.10]

## s.12 Reporting entities, STRs and the Record Rules, 2005 · SM short essay 3

### OBLIGATIONS OF A REPORTING ENTITY (s.12)

**Reporting entity** = a banking company, financial institution, intermediary, or a person carrying on a **designated business or profession**. It must: [SM 406]

a. keep a **record of all prescribed transactions** so that each can be reconstructed;
b. **furnish** information on them to the **Director (FIU)** in time;
c. **verify the identity** of its clients;
d. **identify the beneficial owner** of its clients;
e. keep records of identity documents and account files, and transaction records, for **five years**;
f. for **five years after the relationship ends** or the account is closed, whichever is later.

### PML (MAINTENANCE OF RECORD) RULES, 2005 (REVISED MARCH 2023)

Records of: (a) **cash transactions above ₹10 lakh** (or foreign-currency equivalent); (b) **integrated series** of cash transactions below ₹10 lakh in a month; (c) receipts of ₹10 lakh and more; (d) all transactions with **counterfeit currency**; (e) all **suspicious transactions**, in cash or otherwise; (f) **cross-border wire transfers** above **five lakh rupees** where the origin or destination is in India; (g) purchase or sale of **immovable property of fifty lakh rupees** or more registered by the entity (SM MCQ 1: all of the above). [SM 408]

- A **principal officer** reports to the Director, FIU-IND, every month by the **15th of the next month**. [SM 408]

[SM 406]
**STR**: a transaction, in cash or not, that to a person acting in good faith (a) gives **reasonable ground of suspicion** of proceeds of crime; (b) has **unusual or unjustified complexity**; or (c) has **no economic rationale** or bona fide purpose. [SM 407]

- Clients' KYC data go to the **Central KYC Records Registry within 10 days** (SM MCQ 5); the registry was set up in **2015**; the RBI may call for information from it or inspect it. Digital KYC is online and secure. [SM 408]

## M Model answer · key features of the PMLA (Jun'25 Q8(b)): any seven

1. **Offence** defined widely (s.3): any involvement with proceeds of crime, incl. projecting them as untainted.
2. **Punishment** (s.4): RI 3 to 7 years and fine; up to 10 years for NDPS-linked proceeds.
3. **Scheduled (predicate) offences** in Parts A, B and C; one must exist before an investigation.
4. **Attachment and confiscation** of property, confirmed by the **Adjudicating Authority**.
5. **Authorities**: ED investigates and prosecutes; FIU-IND receives and analyses reports.
6. **Reporting entities**: records, KYC, beneficial owner, reports to FIU, five-year retention; STRs.
7. **Special Courts** (Courts of Session) try the offence with connected scheduled offences.
8. **Appellate Tribunal** for appeals; **reciprocal arrangements** with foreign countries.

[SM 403–408]

### The SM's own exercise (SM 409–410)

**MCQs:** 1 records to keep: **all of the above** · 2 FIU = **Financial Intelligence Unit** · 3 Part B value: **one crore** · 4 STR = **suspicious transaction reports** · 5 KYC to the registry within **10** days · 6 **placement** · 7 tried in **special designated courts** ★. **Fill-ins:** authority = **Directorate of Enforcement** · every scheduled offence is a **predicate** offence ★ · maximum imprisonment **7** years (10 for NDPS proceeds) · FIU · STR · cash above ₹**10** lakh · Central KYC Registry **2015** · Record Rules **2005**. [SM 409–410]

## R Revision: numbers

| Rule | Number | Rule | Number |
|---|---|---|---|
| enacted / in force | Jan 2003 / 1 July 2005 | cash transaction record above | ₹10 lakh |
| chapters / sections / Part A paras | 10 / 75 / 28 | cross-border wire / immovable property | ₹5 lakh / ₹50 lakh |
| punishment | RI 3–7 yrs + fine (10 NDPS) | monthly report to FIU by | 15th |
| Part B value | ≥ ₹1 crore | KYC to central registry | 10 days |
| FIU-IND set up | Nov 2004 | record retention | 5 years |
| Tribunal members | chair + 2 | Central KYC Registry | 2015 |