



IPCC – November 2017

THE COMPANIES ACT, 2013

Test Code – INJ 8014

Branch (MULTIPLE) (Date : 11.06.2017)

(50 Marks)

Note: All questions are compulsory.

Question 1(6marks)

- 1) According to Section 46(1) of the Companies Act, 2013, a share certificate once issued under the common seal of the company, specifying the shares held by any person, shall be prima facie evidence of the title of the person to such shares. Therefore, in the normal course the person named in the share certificate is for all practical purposes the legal owner of the shares therein and the company cannot deny his title to the shares. **(1mark)**
- 2) However, a forged transfer is a nullity. It does not give the transferee (M) any title to the shares. Similarly any transfer made by M (to O) will also not give a good title to the shares as the title of the buyer is only as good as that of the seller. **(1mark)**
- 3) Therefore, if the company acts on a forged transfer and removes the name of the real owner (N) from the Register of Members, then the company is bound to restore the name of N as the holder of the shares and to pay him any dividends which he ought to have received (Barton v. North Staffordshire Railway Co. 38 Ch D 456). **(2marks)**
- 4) In the above case, 'therefore, N has the right against the company to get the shares recorded in his name. However, neither M nor O' have any rights against the company even though they are bona fide purchasers. **(1mark)**
- 5) However, since N seems to be the perpetrator of the forgery, he will be liable both criminally and for compensation to M and O. **(1mark)**

Question 2(6marks)

- 1) Buy Back of own Shares: Sources of Funds etc. Under section 68 of the Companies Act, 2013 a company can purchase its own shares or other specified securities subject to fulfillment of prescribed conditions and subject to defined limits and procedures.
- 2) Under the various sub sections of section 68 of the Companies Act, 2013 , in the present case the following facts are note worthy:
 - 3) The Articles permit buy back – This is in order;
 - a) The approval of the members is by way of an ordinary resolution – This is invalid as the resolution required is a special resolution;
 - b) The buyback approved is 30% of the Equity Share Capital – The maximum limit allowed for buy back is 25% of the aggregate of the paid up capital and free reserves. Since the value of free reserves is not mentioned this cannot be commented upon.
 - c) The company plans to pay for the buy back from the proceeds of an earlier equity issue - This is in violation of section 68 (1) of the Act. **(3marks)**

Taking into account the above factors, the questions as asked in the problem can be answered as under:

- a) The company's proposal for buy-back is not in order as it has passed only an ordinary resolution and the out of the proceeds of an earlier equity issue in violation of section 68 (1).
- b) The answer to the second question shall also be the same as the irregularity and contravention will not be affected by the buyback being 20%. **(3marks)**

Question 3(8 marks)

Shelf Prospectus: Section 2 (70) of the Companies Act, 2013 defines a “Prospectus” and includes a red herring prospectus and a shelf prospectus within the definition of “Prospectus”. Further the explanation to section 31 of the Companies Act,2013 defines a shelf prospectus as a prospectus in respect of which the securities or class of securities included therein are issued for subscription in one or more issues over a certain period without the issue of a further prospectus. **(1mark)**

Section 31 of the Act states that any class or classes of companies, as the Securities and Exchange Board may provide by regulations in this behalf, may file a shelf prospectus with the Registrar at the stage of the first offer of securities included therein which shall indicate a period not exceeding one year as the period of validity of such prospectus which shall commence from the date of opening of the first offer of securities under that prospectus, and in respect of a second or subsequent offer of such securities issued during the period of validity of that prospectus, no further prospectus is required. **(1mark)**

From the above, the key features of a shelf prospectus are as under: **(1mark each)**

- a. A shelf prospectus is a prospectus; hence it must comply with all the provisions of Section 26 of the Act which lays down the matters to be included in a prospectus and filing of the same with the Registrar. It must also comply with the other relevant and applicable sections of the Act to a prospectus.
- b. A shelf prospectus may be issued by a class of companies only if and subject to the regulations of SEBI;
- c. A shelf prospectus can have a validity of a maximum period of one year during which time the company may bring out a number of issue of securities, all covered by the same prospectus.
- d. The validity of a shelf prospectus of a maximum period of one year shall commence from the date on opening of the first offer.

A company filing a shelf prospectus with the Registrar shall not be required to file prospectus afresh at every stage of offer of securities by it within a period of validity of such shelf prospectus. **(1/2mark)**

However, under section 31 (2), a company shall be required to file an information memorandum on all material facts relating to new charges created, changes in the financial position of the company as have occurred between the first offer of securities or any previous offer of securities and the succeeding offer of securities and such other changes as may be prescribe, with the Registrar within the prescribed time, prior to the issue of a second or subsequent offer of securities under the shelf prospectus. **(1mark)**

Section 31 (3) states that where an information memorandum is filed every time an offer of securities is made, such memorandum together with the shelf prospectus shall be deemed to be the prospectus. **(1/2mark)**

Question 4(4 marks)

Following are the material facts to be set out in the explanatory statement to be annexed to the Notice of EGM of Glowing Products Ltd. as per Section 102(1) of Companies Act, 2013:

1. the nature of concern or interest, financial or otherwise, if any, in respect of each items of-
 - a. every director and the manager, if any;
 - b. every other key managerial personnel; and
 - c. relatives of the persons mentioned in sub-clauses (i) and (ii);
2. Any other information and facts that may enable members to understand the meaning, scope and implications of the items of business and to take decision thereon. **(2 marks)**

Further, where any item of special business to be transacted at a meeting of the company relates to or affects any other company, the extent of shareholding interest in that other company of every promoter, director, manager, if any, and of every other key managerial personnel of the first mentioned company shall, if the extent of such shareholding is not less than two percent of the paid up share capital of that company, also be set out in the statement. **(2 marks)**

Question 5 (4 marks)

Section 101 of the Companies Act, 2013 dealing with Notice of meeting, states that a general meeting of a company may be called by giving at least clear 21 days' notice.

However, the Companies Act, 2013 does not prescribe the time limit between the date of approval of financial statements by the Board of Directors of a company and the date of notice of Annual General Meeting. **(2marks)**

Hence, in the given question, the Board of directors of KMP Ltd. should ensure that the gap between the board meeting in which the financial statements are approved and the AGM, should have a minimum gap of 21 clear days (in order to ensure at least 21 days' clear notice), unless the meeting is at a shorter notice. **(2marks)**

Question 6 (8 marks)

Under section 71 (5) of the Companies Act, 2013, no company shall issue a prospectus or make an offer or invitation to the public or to its members exceeding five hundred for the subscription of its debentures, unless the company has, before such issue or offer, appointed one or more debenture trustees and the conditions governing the appointment of such trustees shall be such as may be prescribed. **(1 mark)**

The rules framed under the Companies Act for the issue of secured debentures provide that before the appointment of debenture trustee or trustees, a written consent shall be obtained from such debenture trustee or trustees proposed to be appointed and a statement to that effect shall appear in the letter of offer issued for inviting the subscription of the debentures. **(1 mark)**

Further according to the rules, no person shall be appointed as a debenture trustee, if he-

- (i) Beneficially holds shares in the company;
- (ii) Is a promoter, director or key managerial personnel or any other officer or an employee of the company or its holding, subsidiary or associate company;
- (iii) Is beneficially entitled to moneys which are to be paid by the company otherwise than as remuneration payable to the debenture trustee;
- (iv) Is indebted to the company, or its subsidiary or its holding or associate company or a subsidiary of such holding company;
- (v) Has furnished any guarantee in respect of the principal debts secured by the debentures or interest thereon;
- (vi) Has any pecuniary relationship with the company amounting to two per cent. or more of its gross turnover or total income or fifty lakh rupees or such higher amount as may be prescribed, whichever is lower, during the two immediately preceding financial years or during the current financial year;
- (vii) is a relative of any promoter or any person who is in the employment of the company as a director or key managerial personnel;

(3 marks)

Thus based on the above provisions answers to the given questions are:

- (i) A shareholder who has no beneficial interest can be appointed as a debenture trustee.
- (ii) A creditor whom company owes Rs.499 cannot be so appointed. The amount owed is immaterial.
- (iii) A person who has given guarantee for repayment of principal and interest thereon in respect of debentures also cannot be appointed as a debenture trustee.

(3 marks)

Question (8 marks)

According to Section 13 (1) of the Companies Act, 2013, a company may, by special resolution, and after complying with the procedure specified in this section alter the provisions of its Memorandum. **(1 mark)**

The Name Clause in the Memorandum states the name of the company. It can be changed in the following manner: **(1 mark each)**

1. Passing of the Special Resolution of members at a duly convened general meeting;
2. Hence, in order to convene the general meeting it will be preceded by a Board Meeting
3. The change in name must be in accordance with the provisions of Section 4 (2) and (3). These sub sections prohibit a company from registering with a name similar to an existing company's name or with names listed as undesirable by the Act.
4. After the approval of members the approval of the Central Government, must also be obtained.
5. The approval of the Central Government shall not be necessary when the name change is merely to delete or add the word "Private" before the word "Limited" in the name consequent upon conversion of the company from a public to a private company or vice versa;
6. The documents are required to be filed with the Registrar, who will then register the new name in place of the old name of the company and issue a fresh certificate of incorporation in the new name;
7. The new name will be effective only on and from the date of issue of the new certificate of incorporation by the Registrar as above.

Question 8 (6 marks)(1 mark each)

- 1) The Companies Act, 2013 vide sections 34 and 35 lay down the criminal and civil liabilities of the guilty parties in case of mis-statements and misleading inclusions and omissions in a prospectus. Further, section 36 lays down the punishment for fraudulently inducing persons to invest moneys.
- 2) However, the present case before us is not in respect of liability for a possible misstatement but on the right of the allottee to avoid the contract of purchasing the shares from the company. In order to decide this, key factor to determine, is if any material misrepresentation or concealment of a material fact has taken place and is such misrepresentation is fraudulent.
- 3) The non disclosure of the fact that dividends were paid out of capital profits is a concealment of material fact as a company is normally required to distribute dividend only from trading or revenue profits and under exceptional circumstances can do so out of capital profits. Hence, a material misrepresentation has been made.
- 4) The question here is a direct issue arising from the consequence of misrepresentation on the contract and is governed by the Indian Contract Act, 1872.
- 5) Section 19 of the Indian Contract Act, 1872 states that when consent to an agreement is caused by coercion, fraud or misrepresentation, the agreement is a contract voidable at the option of the party whose consent was so caused.
- 6) Hence, in the given case the allottee can avoid the contract of allotment of shares. (Rex V. Lord Kylsant).
