

Note: Question 1 is compulsory. Attempt any five from the rest.

Question 1

- (A) According to the provisions of Section 184 of the Indian Contract Act, 1872, as between the principal and a third person, any person, even a minor may become an agent. But no person who is not of the age of majority and of sound mind can become an agent, so as to be responsible to his principal. Thus, if a person who is not competent to contract is appointed as an agent, the principal is liable to the third party for the acts of the agent. Thus, in the given case, Dharmesh gets a good title to the watch . Mitesh is not liable to Ramesh for his negligence in the performance of his duties. **(5 marks)**

(B)

The problem stated in the question is based on the provisions of the Negotiable Instruments Act, 1881 as contained in Section 53. The section provides: 'Once a negotiable instrument passes through the hands of a holder in due course, it gets cleansed of its defects provided the holder was himself not a party to the fraud or illegality which affected the instrument in some stage of its journey. Thus any defect in the title of the transferor will not affect the rights of the holder in due course even if he had knowledge of the prior defect provided he is himself not a party to the fraud. (Section 53).

Thus applying the above provisions it is quite clear that S who originally induced Y in obtaining the bill of exchange in question fraudulently, cannot succeed in the case. The reason is obvious as S himself was a party to the fraud.

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- (C) **Section 203(3) of the Companies Act, 2013** provides that whole time key managerial personnel shall not hold office in more than one company except in its subsidiary company at the same time. With respect to the issue that whether a whole time KMP of holding company be appointed in more than one subsidiary companies or can be appointed in only one subsidiary company. **(3 Marks)**

It can be noted that Section 13 of General Clauses Act, 1897 provides that the word 'singular' shall include the 'plural', unless there is anything repugnant to the subject or the context. Thus, a whole time key managerial personnel may hold office in more than one subsidiary company as per the present law. **(2 marks)**

- (D) Yes, (being a fundamental right under the Constitution of India to go for legal proceedings) the registration of the company can be challenged but it will not in any way affect or cancel the registration of the company and the Memorandum and Articles. **(2 marks)**

Section 10 (1) of the Companies Act, 2013 states that subject to the provisions of the Act, the Memorandum and Articles shall, when registered, bind the company and the members thereof, to the same extent as if they respectively had been signed by the company and by each member, and contained covenants on its and his part to observe all the provisions of the Memorandum and of the Articles. **(3 marks)**

Question 2

(A)

According to the Section 125 of the Indian Contract Act, 1872 the indemnity holder i.e., promisee in a contract of indemnity, acting within the scope of his authority, is entitled to recover from the promisor :

(1) all damages which he may be compelled to pay in any suit in respect of any matter to which the promise to indemnify applies;

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(2) <u>all costs</u> which he may be compelled to pay in any such suit, if in bringing or defending it, he did not contravene the orders of the promisor, and acted as it would have been prudent for him to act in the absence of any contract of indemnity, or if the promisor authorised him to bring or defend the suit.		2
(3) <u>all sums</u> which he may have paid under the terms of any compromise of any such suit, if the compromise was not contrary to the orders of the promisor, and was one which it would have been prudent for the promisee to make in the absence of any contract of indemnity, or if the promisor authorised him to compromise the suit.		1
Section 125 is by no means exhaustive, which deals only with his rights in the event of his being sued. The indemnity holder has other rights besides those mentioned above. If he has incurred a liability and that liability is absolute he is entitled to call upon his indemnifier to save him from that liability and to pay it off.		1

(B) Section 5 (1) of the Companies Act, 2013 states that the Articles of a company contain the regulations for the management of a company. Further section 5 (2) provides that the Articles of a company shall contain all matters that are prescribed under the Act and also such additional matters as may be considered necessary for the management of the company. (

Removal of Law Officer : The Memorandum and Articles of Association of a company are binding upon company and its members and they are bound to observe all the provisions of memorandum and articles as if they have signed the same [Section 10(1)].

However, the company and members are not bound to outsiders in respect of anything contained in memorandum/articles by which such outsiders have been given any rights. This is based on the general rule of law that a stranger to a contract cannot acquire any right under the contract.

In this case, Articles conferred a right on 'X', the law officer that he shall not be removed except on the ground of proved misconduct. In view of the legal position explained above, 'X' cannot enforce the right conferred on him by the articles against the company. Hence the action taken by the company (i.e. removal of 'X' even though he was not guilty of misconduct) is valid.

However, by altering the Articles by a special resolution under section 14 of the Act and Mr. X can be removed.

(C)

Comprehensive rules and regulations have been incorporated into the Companies Act, 2013 in respect of this basic document which is the only source of vital information for the investors to ascertain the soundness or otherwise of the company. Since the prospectus is intended to save the investing public from victimisation, the Legislature has aimed at securing the fullest disclosure of all material and essential particulars and laying the same before all the prospective buyers of shares and imposing stringent liabilities for violations. **(2 Marks)**

Briefly the rules and regulations are as follows: **(4 marks)**

Matters to be stated in a Prospectus – In order to provide a thorough and comprehensive information on all aspects of the company and the proposed issue, section 26 (1) of the Companies Act, 2013 lists down a large list of items that must be stated in the Prospectus.

Registration of prospectus – Section 26 (4) provides that no prospectus shall be issued by or on behalf of a company or in relation to an intended company, unless on or before the date of its publication, there has been delivered to the Registrar for registration, a copy thereof signed by every person or his duly authorized representative, who is named therein as a director or proposed director of the company.

Under sub section (7) it is provided that the Registrar shall not register the prospectus unless the requirements for registration under section 26 are complied with and the prospectus is accompanied by the consent of all the persons named in the prospectus.

Approval of prospectus by various agencies : The draft prospectus has to be approved by various agencies before it is filed with the ROC of the concerned

State.

The lead financial institution underwriting the issue, if applicable : The draft prospectus is vetted by SEBI to ensure adequacy of disclosures. However, vetting by SEBI does not amount to approval of prospectus. SEBI does not take any responsibility for the correctness of the statements made or opinions expressed in the prospectus.

Question 3

(A) (8 marks)

<u>Bailment</u> is defined as <u>an act whereby goods are delivered by the person to another for some purpose on a contract that the goods shall, when the purpose is accomplished, be returned or otherwise disposed of according to the directions of the person delivering them.</u> <u>Bailor</u> – the <u>person who delivers the goods</u> <u>Bailee</u> - the <u>person to whom the goods are delivered.</u>		2
Duties (i) Bailor has to <u>disclose all the facts/faults</u> about bailed goods to bailee. (ii) Under <u>gratuitous bailment</u> , Bailor has to <u>reimburse expenses incurred by Bailee</u> , if any. (iii) Bailor has to <u>compensate the loss</u> on bailed goods to Bailee, if any. (iv) Bailor has to <u>accept the goods after purpose is accomplished.</u>		2
Rights (i) To enforce <u>bailee’s duties such as right to claim damages</u> , compensation, if any. (ii) To <u>terminate the contract of bailment.</u> (iii) To <u>demand back goods.</u> (iv) To <u>claim increase or profit from goods bailed.</u>		2
Different forms of Bailment: Following are the <u>popular forms</u> of bailment (1) <u>Delivery of goods by one person to another to be held for the bailor’s use.</u> (2) Goods given to a <u>friend for his own use without any charge</u> (3) <u>Hiring of goods.</u> (4) Delivering goods <u>to a creditor to serve as security for a loan.</u> (5) Delivering goods for <u>repair with or without remuneration.</u> (6) Delivering goods for <u>carriage.</u>		2 for any 4

(B) Irregular allotment : The Companies Act, 2013 does not separately provide for the term “Irregular Allotment” of securities. Hence, one will have to examine the requirements of a proper issue of securities and consider the consequences of non fulfilment of those requirements.

In broad terms, an allotment of shares is deemed to be irregular when it has been made by a company in violation of Sections 23, 26, 39 and 40. Irregular allotment therefore arises in the following instances:

- Where a company does not issue a prospectus in a public issue as required by section 23; or
- Where the prospectus issued by the company does not include any of the matters required to be included therein under section 26 (1), or the information given is misleading, faulty and incorrect; or
- Where the prospectus has not been filed with the Registrar for registration under section 26 (4);
- The minimum subscription as specified in the prospectus has not been received in terms of section 39; or
- The minimum amount receivable on application is less than 5% of the nominal value of the securities offered or lower than the amount prescribed by SEBI in this behalf; or
- In case of a public issue, approval for listing has not been obtained from one or more of the recognized stock exchanges under section 40 of the Companies Act,

2013 **(4 marks)**

Effects of irregular allotment : The consequences of an irregular allotment depend on the nature of irregularity. However, the Companies Act, 2013 does not mention (unlike the previous Companies Act) that in case of an irregular allotment the contract is voidable at the option of the allottee.

Under section 26 (9) of the Companies Act, 2013 if a prospectus is issued in contravention of the provisions of section 26, the company shall be punishable with fine which shall not be less than fifty thousand rupees but which

may extend to three lakh rupees and every person who is knowingly a party to the issue of such prospectus shall be punishable with imprisonment for a term which may extend to three years or with fine which shall not be less than fifty thousand rupees but which may extend to three lakh rupees, or with both.

Similarly, in case the company has not received the minimum subscription amount within 30 days of the date of issue of the prospectus, it must refund the application money received by it within the stipulated time. Any allotment made in violation of this will be void and the defaulting company and officers will be liable to further punishment as provided in section 39 (5).

Under section 40 (5) any default made in respect of getting the approval to listing of securities in one or more recognized stock exchange in case of a public issue, will render the company punishable with a fine which shall not be less than five lakh rupees but which may extend to fifty lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than fifty thousand rupees but which may extend to three lakh rupees, or with both.

Hence, under various provisions of the Companies Act, 2013 stringent punishment has been provided for against irregular allotment of securities but the option of going ahead with such allotment even if desired by the allottee is not specifically permitted. (4 marks)

Question 4

(A) (6 marks)

<p><u>Holder in Due Course:</u> It means <u>any person</u> who, for consideration became its <u>possessor</u> before the <u>amount</u> mentioned in it <u>became payable</u>. In the case of an instrument payable to order, '<u>holder in due course</u>' means <u>any person</u> who became the <u>payee</u> or <u>endorsee</u> of the instrument before the amount mentioned in it became payable. In both the cases, he <u>must receive the instrument without having sufficient cause to believe that any defect existed</u> in the title of the person from whom he derived his title. In other words, <u>holder in due course</u> means a holder who takes the instrument <u>bona fide for value</u> before it is overdue, and without any notice of defects in the title of the person, who transferred it to him.</p>		3
<p>Thus, a <u>person</u> who <u>claims to be 'holder in due course'</u> is <u>required to prove that:</u></p> <ol style="list-style-type: none"> <u>on paying a valuable consideration</u>, he <u>became either the possessor</u> of the instrument if payable to order; he had <u>come into the possession</u> of the <u>instrument before the amount due there under became actually payable</u>; and he had <u>come to possess the instrument without having sufficient cause to believe that any defect existed</u> in the title of transferor's from whom derived his title. 		
<p>Distinction between Holder and Holder in Due Course:</p> <ol style="list-style-type: none"> A holder may become the possessor or payee of an instrument even without consideration, whereas a holder in due course is one who acquires possession for consideration. A holder in due course as against a holder must become the possessor payee of the instrument before the amount thereon become payable. A holder in due course as against a holder must have become the payee of the instrument in good faith i.e., without having sufficient cause to believe that any defect existed in the transferor's title. 		3

Holder in Due Course: It means any person who, for consideration became its possessor before the amount mentioned in it became payable. In the case of an instrument payable to order, 'holder in due course' means any person who became the payee or endorsee of the instrument before the amount mentioned in it became payable. In both the cases, he must receive the instrument without having sufficient cause to believe that any defect existed in the title of the person from whom he derived his title. In other words, holder in due course means a holder who takes the instrument bona fide for value before it is overdue, and without any notice of defects in the title of the person, who transferred it to him.

Thus, a person who claims to be 'holder in due course' is required to prove that:

- on paying a valuable consideration, he became either the possessor of the instrument if payable to order;
- he had come into the possession of the instrument before the amount due there under became actually payable; and
- he had come to possess the instrument without having sufficient cause to believe that any defect existed in the title of transferor's from whom derived his title.

Distinction between Holder and Holder in Due Course:

1. A holder may become the possessor or payee of an instrument even without consideration, whereas a holder in due course is one who acquires possession for consideration.
2. A holder in due course as against a holder must become the possessor payee of the instrument before the amount thereon become payable.
3. A holder in due course as against a holder must have become the payee of the instrument in good faith i.e., without having sufficient cause to believe that any defect existed in the transferor's title.

(B) Alteration of Capital [Section 61 (1) read with section 13 of the Companies Act, 2013]: Under section 61 (1) a limited company having a share capital may, if authorized by its Articles, alter its Memorandum in its general meeting as under : **(3 marks)**

- (i) it may increase its authorized share capital by such amount as it thinks expedient;
- (ii) it may consolidate and divide all or any of its share capital of a larger amount than its existing shares
- (iii) convert all or any of its paid up shares into stock and reconvert that stock into fully paid shares of any denomination
- (iv) sub-divide the whole or any part of its shares into shares of smaller amount than is fixed by the Memorandum
- (v) cancel those shares which, at the time of passing of the resolution in that behalf have not been taken or agreed to be taken by any person, and diminish the amount of its share capital by the amount of the shares so cancelled.

Further, under section 64 where a company alters its share capital in any of the above mentioned ways, the company shall file a notice in the prescribed form with the Registrar within a period of thirty days of such alteration or increase or redemption, as the case may be, along with an altered memorandum. **(3 marks)**

Section 13 provides for the procedure to be followed for alteration of the Memorandum, as under :

- a. A special resolution must be passed to effect the alteration. For this purpose a Board Meeting must be held to convene a general meeting of the members and all legal provisions in this behalf followed including the circulation of a detailed explanatory note on the proposed change alongwith the notice for the general meeting;
- b. The company must file with the Registrar the special resolution passed by the company to effect an alteration in the capital clause of the Memorandum;
- c. No alteration to the Memorandum will have effect unless it has been registered with the Registrar as above.

(C) "Eligible company" means a public company as referred to in sub-section (1) of section 76, having a net worth of not less than one hundred crore rupees or a turnover of not less than five hundred crore rupees and which has obtained the prior consent of the company in general meeting by means of a special resolution and also filed the said resolution with the Registrar of Companies before making any invitation to the Public for acceptance of deposits : **(3 marks)**

However, an eligible company, which is accepting deposits within the limits specified under clause (c) of sub-section (1) of section 180, may accept deposits by means of an ordinary resolution. **(1 mark)**

Question 5

(A) The rules regarding interpretation of deeds and documents are as follows :

First and the foremost point that has to be borne in mind is that one has to find out what **reasonable man, who** has taken care to inform himself of the surrounding circumstances of a deed or a document, and of its scope and intendments, would understand by the words used in that deed or document.

It is inexpedient to construe the terms of one deed by reference to the terms of another. Further, it is well established that the same word cannot have two different meanings in the same documents, unless the context compels the adoption of such a rule.

The Golden Rule is to ascertain the intention of the parties of the instrument after considering all the words in the documents/deed concerned in their ordinary, natural sense. For this purpose, the relevant portions of the document have to be considered as a whole. The circumstances in which the particular words have

been used have also to be taken into account. Very often, the status and training of the parties using the words have also to be taken into account as the same words maybe used by a ordinary person in one sense and by a trained person or a specialist in quite another sense and a special sense. It has also to be considered that very many words are used in more than one sense. It may happen that the same word understood in one sense will give effect to all the clauses in the deed while taken in another sense might render one or more of the clauses ineffective. In such a case the word should be understood in the former and not in the latter sense.

It may also happen that there is a conflict between two or more clauses of the same documents. An effect must be made to resolve the conflict by interpreting the clauses so that all the clauses are given effect. If, however, it is not possible to give effect of all of them, then it is the earlier clause that will override the latter one.

(B)

- (i) Section 127 of the Companies Act, 2013 provides for punishment for failure to distribute dividend on time. One of such situations is where a shareholder has given directions to the company regarding the payment of the dividend and those directions cannot be complied with and the same has not been communicated to her.

In the given situation, the company has failed to communicate to the shareholder Mrs. Sheela about non-compliance of her direction regarding payment of dividend. Hence, the penal provisions under section 127 will be applicable. **(3 marks)**

- (ii) Section 127, inter-alia, provides that no offence shall be deemed to have been committed where the dividend could not be paid by reason of operation of law.

In the present circumstance, the dividend could not be paid because it was not allowed to be paid by the court until the matter was resolved about succession. Hence, there will not be any liability on the company and its Directors etc. **(3 marks)**

(C) The auditor is right. Theoretically, accounts are presented to auditors only after they are approved by the Board and signed by authorized persons. The auditor is only expected to submit his report on the accounts presented to him for audit after conducting an examination of the necessary documents, analyzing relevant information and test checking accounting records in order to be able to form an opinion of the financial statements presented to him. In practice, the checking of accounts is already completed before accounts are approved by the Board. Auditor informally approves the draft account with notes etc., before the accounts are approved by the Board. However, auditor signs the accounts only after these are approved by Board and signed by persons authorized by Board of the company. **(4 marks)**

Question 6

(A)

- (i) The appointment and re-appointment of auditor of a Government Company or a government controlled company is governed by the provisions of section 139 of the Companies Act, 2013 which are summarized as under :

The first auditor shall be appointed by the Comptroller and Auditor General of India within 60 days from the date of incorporation and in case of failure to do so, the Board shall appoint auditor within next 30 days and on failure to do so by Board of Directors, it shall inform the members, who shall appoint the auditor within 60 days at an extraordinary general meeting (EGM), such auditor shall hold office till conclusion of first Annual General Meeting.

In case of subsequent auditor for existing government companies, the Comptroller & Auditor General of India shall appoint the auditor within a period of 180 days from the commencement of the financial year

and the auditor so appointed shall hold his position till the conclusion of the Annual General Meeting. **(3 marks)**

(ii) The situation as stated in the question relates to the creation of a casual vacancy in the office of an auditor due to resignation of the auditor before the AGM in case of a company other government company. Under section 139 (8)(i) any casual vacancy in the office of an auditor arising as a result of his resignation, such vacancy can be filled by the Board of Directors within thirty days thereof and in addition the appointment of the new auditor shall also be approved by the company at a general meeting convened within three months of the recommendation of the Board and he shall hold the office till the conclusion of the next annual general meeting. **(3 marks)**

(iii) The Companies Act, 2013 categorizes companies into government companies and non Government Companies and lists down the provisions relating to appointment, of auditors as per this classification. Hence, in the given case as the total shareholding of the three institutions adds up to 30% of the subscribed capital of the company it is not a government company. Hence, the provisions applicable to non-government companies in relation to the appointment of auditors shall apply. **(2 marks)**

(A) According to Section 73 (2) of the Companies Act, 2013, a company may, subject to the passing of a resolution in general meeting and subject to such rules as may be prescribed in consultation with the Reserve Bank of India, accept deposits from its members on such terms and conditions, including the provision of security, if any, or for the repayment of such deposits with interest, as may be agreed upon between the company and its members, subject to the fulfilment of the following conditions, namely :

(a) issuance of a circular to its members including therein a statement showing the financial position of the company, the credit rating obtained, the total number of depositors and the amount due towards deposits in respect of any previous deposits accepted by the company and such other particulars in such form and in such manner as may be prescribed;

(b) filing a copy of the circular along with such statement with the Registrar within 30 days before the date of issue of the circular;

(c) depositing such sum which shall not be less than fifteen per cent. of the amount of its deposits maturing during a financial year and the financial year next following, and kept in a scheduled bank in a separate bank account to be called as deposit repayment reserve account;

(d) providing such deposit insurance in such manner and to such extent as may be prescribed;

(e) certifying that the company has not committed any default in the repayment of deposits accepted either before or after the commencement of this Act or payment of interest on such deposits; and providing security, if any for the due repayment of the amount of deposit or the interest thereon including the creation of such charge on the property or assets of the company : Where a company does not secure the deposits or secures such deposits partially, then, the deposits shall be termed as “unsecured deposits” and shall be so quoted in every circular, form, advertisement or in any document related to invitation or acceptance of deposits. **(5 marks)**

Exceptions : (3 marks)

1. In case of private company - Points (a) to (e) above shall not apply to private Companies which accepts from its members monies not exceeding 100%, of aggregate of the paid up share capital and free reserves, and such company shall file the details of monies so accepted to the Registrar in such manner as may be specified.

2. In case of Specified International Financial Service Centre (IFSC) Public Company - Points (a) to (e) above shall not apply to a Specified IFSC public company which accepts from its members, monies not exceeding 100% of aggregate of the paid up share capital and free reserves, and such company shall file the details of monies so accepted to the Registrar in such manner as may be specified. Hence, Atul Ltd. can accept deposits from its members by following the above condition and regulations.

(C) The Finance Manager of Belt Ltd is of the opinion that before declaration of dividends it would not be necessary to set off the carried forward amount of debit balance in the Profit & Loss Account against current Revenue Profit but the same could be set off against Revaluation Reserve. Do you agree?

In a Company, Fixed Assets have been revalued and there has been resulting Surplus of ` 2, 00,000, which is transferred to Revaluation Reserve. The Company has a debit balance in Profit and Loss Account ` 1, 20,000 as Accumulated Brought Forward Losses. The Company has adjusted this loss balance against Revaluation Reserve. Give your comments.

Fixed Assets have been revalued and the resultant Surplus adjusted against Brought Forward Losses. Comment.

At the beginning of the year, the Company has a Capital of ` 15 Crores, General Reserve of ` 1 crore and Revaluation Reserve of ` 6 crores. In the year 2013-2014 under audit, the Company has incurred a loss of ` 5.5 Crores. The Company proposes to adjust the loss against the Revaluation Reserves. Comment **(4 marks)**

Question 7

(A) Interpretation of the words “Means” and “Includes” in the definitions- The definition of a word or expression in the definition section may either be restricting of its ordinary meaning or may be extensive of the same. When a word is defined to ‘mean’ such and such, the definition is ‘prima facie’ restrictive and exhaustive, we must restrict the meaning of the word to that given in the definition section.

But where the word is defined to ‘include’ such and such, the definition is ‘prima facie’ extensive, here the word defined is not restricted to the meaning assigned to it but has extensive meaning which also includes the meaning assigned to it in the definition section.

Example—

Definition of Director [section 2(34) of the Companies Act, 2013]—Director means a director appointed to the board of a company. The word “means” suggests exhaustive definition.

Definition of Whole time director [Section 2(94) of the Companies Act, 2013]— Whole time director includes a director in the whole time employment of the company. The word “includes” suggests extensive definition. Other directors may be included in the category of the whole time director.

(B) The term charge has been defined in section 2 (16) of the Companies Act, 2013 as an interest or lien created on the property or assets of a company or any of its undertakings or both as security and includes a mortgage. Every company is under an obligation to keep at its registered office a register of charges and enter therein all charges specifically affecting property of the company and all floating charges on the undertaking or any property of the company. **Punishment for contravention** – According to section 86 of the Companies Act, 2013, if a company makes any default with respect to the registration of charges covered under chapter VI, a penalty shall be levied, ranging from ` 1 lakh to 10 lakhs. Every defaulting officer is punishable with imprisonment for a term not exceeding 6 months or fine which shall not be less than 25,000 rupees, but not exceeding 1 lakh rupees or both. **(6 marks)**

(C) The Companies Act, 2013 under section 13 provides for the process of altering the Memorandum of a company. Since the location or Registered Office clause in the Memorandum only names the state in which its registered office is situated, a change in address from Mumbai to Pune, does not result in the alteration of the Memorandum and hence the provisions of section 13 (and its sub sections) do not apply in this case. However, under section 12 (5) of the Act which deals with the registered office of company, the change in registered office from one town or city to another in the same state, must be approved by a special resolution of the company. Further, presuming that the Registrar will remain the same for the whole state of Maharashtra, there will be no need for the company to seek the confirmation to such change from the Regional Director. **(4 marks)**
