

THE COMPANIES ACT, 1956

Unit – 1 : Preliminaries

Question 1

Briefly discuss the provisions relating to constitution of National Company Law Tribunal and National Company Law Appellate Tribunal. (May 2007)

Answer

Part VI-A has been introduced into the Companies Act, 1956 by the Companies (Second Amendment Act, 2002). Its enforcement will mean repeal of the Sick Industrial Companies (Special provisions) Act, 1985 and also abolition of the Board of Industrial and Financial Reconstruction (BIFR). Such cases will go before the National Company Law Tribunal. Section 424A provides for such reference. The Board of Directors of a sick industrial company have to make a reference to the Tribunal. They have to prepare a scheme for its revival and rehabilitation and submit to the tribunal along with an application containing such particulars as may be prescribed. The Tribunal thereafter has to enquire with working of sick industrial companies. The Tribunal is empowered to make suitable orders on completion of the Enquiry (see Section 424-B and 424-C).

The National Company Law Appellate Tribunals have been constituted by central Government by notification with official gazette. Any person aggrieved by an order of the Tribunal, can within 45 days file an appeal before the National Company Law Appellate Tribunal, which will pass orders after giving opportunity of hearing to the aggrieved party.

Question 2

Mr. Ram Lal and his friend desire to incorporate a Public Company and approach you for help. Advise. (May 2007)

Answer

1. A name must be got allotted out of a choice of three.
2. Seven members (minimum) must be ready to sign as subscribers to the MOA and AOA.
3. MOA and AOA with necessary objects and clauses should be prepared on stamp paper according to State Stamp Act.

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4. Consent must be given in Form No. 32 for becoming a Director. List of directors must also be filed.
5. Form No. 18 showing address of the registered office is also another document.
6. Form No. 1 – Declaration by a Professional or Director is also necessary on the requisite stamp paper.
7. The name available letter should be filed in Original.
8. A power of attorney on non-judicial stamp paper for making corrections and receiving Incorporation Certificate is necessary.
9. Fees for registration of a company depending upon the authorised capital must also be paid.

After satisfaction of the above requirements, the ROC issues a certificate stating that the public company has been incorporated.

Question 3

Explain the doctrine of 'Indoor Management' in brief.

The Secretary of a Company issued a share certificate to 'A' under the Company's seal with his own signature and the signature of a Director forged by him. 'A' borrowed money from 'B' on the strength of this certificate. 'B' wanted to realise the security and requested the company to register him as a holder of the shares. Explain whether 'B' will succeed in getting the share registered in his name. (May 2007)

Answer

The doctrine of Indoor Management as discussed in the *Royal British Bank vs. Turquand (1956) 6E&B 327*. In this case the directors of Royal British Bank also gave a bond to Turquand. The Article empowered the directors to issue such bonds under the authority of a proper resolution. In fact no such resolution was passed. Notwithstanding that, it was held that Turquand could sue on the bonds on the ground that he was entitled to assume that the resolution had been duly passed. Thus the persons dealing with the company are entitled to assume that the acts of the directors or the officers of the company are validly performed, if they are within the scope of their apparent authority. But this doctrine is not applicable where the person dealing with the company has notice of irregularity or where the person dealing with the company is put upon inquiry or when an instrument purporting to be enacted on behalf of the company is a forgery.

In the instant problem the doctrine of Indoor Management can apply only in case of irregularities which might otherwise affect the transaction, but it cannot apply to forgery which must be regarded as nullity. Hence 'B' will not succeed in getting the share registered in his name.

Question 4

What is meant by 'Pre-Incorporation Contracts'? Can these contracts be enforced by the prospective company after its incorporation against the third parties with whom the promoters had entered into certain contracts? Explain. (November 2007)

Answer

Pre-incorporation Contracts and its Enforcement: Pre-incorporation Contracts are those contracts which are entered into, by the promoters on behalf of a prospective company, before it has come into existence e.g. with the proprietor of business to sell it to the prospective company. Since a company comes into existence from the date of its incorporation, it follows that any act purporting to be performed by it prior to that date is of no effect so far as the company is concerned. Hence the vendor cannot sue or be sued by the company thereof, after its incorporation.

After incorporation, the company may adopt the preliminary agreement. But this must be, by novation. However, in order to facilitate companies to adopt pre-incorporation contracts, special provisions are made in Sections 15 and 19 of the Specific Relief Act, 1963. Accordingly, Pre-incorporation Contracts can be enforced by the company, if the contract is for the purposes of the company, the contract is warranted by the terms of its incorporation and is within the scope of the company's objects as given in the Memorandum of Association and the company has accepted the contract and has communicated such acceptance to the other party.

Question 5

Mr. V, alongwith six other persons desires to float a company for charitable purposes, as permissible under Section 25 of the Companies Act, 1956. He seeks your advise about the procedure to be followed to give effect to the above proposal. Advise him.

(November 2007)

Answer

Company for charitable purposes: (Section 25 of the Companies Act, 1956)

According to Section 25 of the Companies Act, 1956 the procedure to be followed to give effect to the said proposal is as follows:

1. Mr. V, must mobilise six other persons who are majors and sound mind to sign MOA and AOA which may be of its own or as in Table "C" or "D" of the Companies Act.
2. The company may be a Limited Company with share capital or a company limited by guarantee.
3. In no case the profits of the company can be distributed in the forms of dividends on bonus shares.
4. All the profits of the company should be used only for welfare purposes and company's progress. These factors must be incorporated in AOA.

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5. Out of the three names chosen by the promoters for the name of the company one should be used. If it is not available the proposals repeated by filing form no. 1A.
6. After getting the name from the ROC, the draft MOA and AOA must be got approved by Regional Director who has been delegated the powers by the Central Government.
7. Three copies of a approved MOA and AOA alongwith the registration and filing fee, documents like form 1,18,32 and consent etc. must be submitted.
8. A power of attorney in favour of Practicing CA/CS/ICWA or an advocate for presentation before ROC to make corrections and collect incorporation certificate must also be filed on non judicial stamp paper.
9. The company becomes operative on incorporation.

Question 6

Board of Directors of a private company decided to convert it into a public company. State the steps to be taken for such conversion in order to comply with the requirements under the Companies Act, 1956. (November 2007)

Answer

Conversion of a Private Company into a Public Company

The conversion of the private company into a public company is by choice under Section 44 of the Companies Act, 1956.

The following steps are required to be taken for such conversion:

- (i) Board must fix the date for General Meeting for the purpose of making necessary alternation in the Articles of Association and Memorandum of Association.
- (ii) Hold the General Meeting and pass a special resolution altering the articles in such a manner that they no longer include the provisions of Section 3(1) (iii) which are required to be included in the articles of a company in order to constitute it a private company. The company ceases to be a private company from the date of alteration. The articles are required to be altered so as to bring there in line with the provisions of the Act as applicable to public company.
- (iii) Special resolution to change the name of the company, so as to delete the word 'private' from the name of the company and to alter the Memorandum of Association for that purpose
- (iv) File copies of the special resolution and prospectus or statement in lieu of prospectus within 30 days from the date of general meeting and obtain a fresh certificate of incorporation (deleting word 'private' in the name of the company) from Registrar of Companies.
- (v) The company must ensure the minimum number of members is 7, and directors is 3 and the paid up capital is not less than Rs. 5 lakhs.

Question 7

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VD Company Ltd. is registered in Tamil Nadu within the jurisdiction of the Registrar of Companies, Chennai. The company proposes to shift its registered office to a place within the jurisdiction of Registrar of Companies, Coimbatore. State the steps to be taken by the company to give effect to the proposed shifting of its registered office. (May 2008)

Answer

Change of registered office from the jurisdiction of one ROC to another within same State (Section 17-A of the Companies Act, 1956) : In this case the company has to comply with the provisions of Section 17-A of the Companies Act, 1956. The proposed change of registered office from the jurisdiction of ROC, Chennai to ROC, Coimbatore will be effective only after such change is confirmed by the Regional Director who shall communicate the confirmation within 4 weeks from the date of receipt of application.

Certified copy of the confirmation along with the attested copy of the Memorandum of Association must be filed with ROC under whose jurisdiction the Registered Office is being shifted within 2 months from the date of confirmation. The Registrar will issue Registration certificate within one month of filing the documents. The certificate shall be conclusive evidence that all the requirements of the Companies Act, 1956 have been complied with.

Question 8

What will be the consequence in case a Private Company incorporated under the provisions of the Companies Act, 1956 defaults in complying with conditions constituting Private Company in terms of Section 3 (1) (iii) of the Companies Act, 1956.

(November 2008)

Answer

Consequence in case of private company acting in contravention of Section 3 (1) (iii) of the Companies Act 1956:

A private company which has been constituted under Section 3(1) (iii) has the following characteristics:

- ◆ minimum 2 members
- ◆ maximum 50, excluding employees and ex-employees who had become members when they were employees
- ◆ minimum 2 directors
- ◆ with restrictions on transferability of shares
- ◆ restrained from inviting public for share capital and from issuing prospectus
- ◆ with minimum paid up capital of Rs.1 lakh
- ◆ prohibited from accepting deposits from persons other than its members, directors and their relatives.

Some other procedural concessions are also given under the Companies Act, 1956.

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In accordance with the provisions of Section 43 of the Companies Act, 1956, if contravention is made against complying with the provisions contained in Section 3 (1) (iii), the company shall lose all the privileges and exemptions conferred on it by the Act, and the provisions of the Act shall apply to it as if it were not a private company. But the Company Law Board may relieve the company from such a consequence if it is satisfied that the failure in compliance with the said requirement was not deliberate but was accidental or inadvertent or that on other grounds it is just and equitable to grant relief.

Question 9

The Articles of a Public Company clearly stated that Mr. A will be the solicitor of the company. The Company in its general meeting of the shareholders resolved unanimously to appoint B in place of A as the solicitor of the company by altering the Articles of Association. Examine, whether the company can do so? State the reasons clearly. (November 2008)

Answer

According to Section 36(1) of the Companies Act, 1956, 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 combined covenants on its and his part to observe all the provisions of the memorandum and articles. Section 36 creates an obligation binding on the company in its dealings with the members but the word "members" in this Section means members in their capacity as members, that is, excluding any relationship which does not flow from the membership itself. Therefore even a member cannot enforce the provisions of articles for his benefit in some other capacity than that of a member.

Section 31 also provides that the company may by special resolution alter its articles. In the given problem the company has changed its articles by passing resolution unanimously and therefore the company can change its articles. The provision of memorandum and articles will bind the members but in the capacity of a member only and even a member may be treated as an outsider. Therefore a member cannot enforce the provisions of articles for his benefit in some other capacity than that of a member. In the given case A will not succeed and the company is empowered to appoint B as a solicitor of the company and may change the articles accordingly. The problem is based upon the decision held in *Eley vs. Positive Govt. Security Life Assurance Co.* (1876).

Question 10

F, an assessee, was a wealthy man earning huge income by way of dividend and interest. He formed three Private Companies and agreed with each to hold a block of investment as an agent for them. The dividend and interest income received by the companies was handed back to F as a pretended loan. This way, F divided his income into three parts in a bid to reduce his tax liability.

Decide, for what purpose the three companies were established? Whether the legal personality of all the three companies may be disregarded? (June 2009)

Answer

The House of Lords in *Salomon Vs Salomon & Co. Ltd.* laid down that a company is a person distinct and separate from its members, and therefore, has an independent separate legal existence from its members who have constituted the company. But under certain circumstances the corporate veil may be lifted by the courts. It means looking behind the corporate façade and disregarding the corporate entity. Where a company is incorporated and formed by certain persons only for the purpose of evading taxes, by taking shelter of the corporate nature, the courts have discretion to disregard the corporate entity in the matter of tax evasion.

(1) The problem asked in the question is based upon the aforesaid facts. The three companies were formed by the assessee purely and simply as a means of avoiding tax and the companies were nothing more than the assessee himself. Therefore the whole idea of Mr. F was simply to split his income into three parts with a view to evade tax.

(2) The legal personality of the three private companies may be disregarded because the companies were formed only to avoid tax liability and the company was nothing more than the assessee himself. It did no business, but was created simply as a legal entity to ostensibly receive the dividend and interest and to handover them over to the assessee as pretended loans. The same was upheld in *Re Sir Dinshaw Maneckji Petit* AIR 1927 Bom.371 and *Juggilal vs. Commissioner of Income Tax* AIR (1969) SC (932).

Question 11

India Cosmetics Limited was a registered company under the Companies Act, 1956. Later on, another company, India Cosmetics and Accessories Limited was formed and registered. There being similarity in the names of both the Companies, India Cosmetics Limited lodged a complaint against India Cosmetics and Accessories Limited, with the Registrar of Companies, stating that there is sufficient similarity between these two names which may mislead or defraud the public. India Cosmetics and Accessories Limited is intending to alter its name.

Advise India Cosmetics and Accessories Limited to alter the name of the Company according to the provisions of the Companies Act, 1956. (June 2009)

Answer

Similarity in the names of Companies

In accordance with Section 22(1) of the Companies Act, 1956, if through inadvertence or otherwise, a company on its first registration or on its registration by a new name, is registered by a name which in the opinion of the Central Government, is identical with, or too nearly resembles, the name by which a company in existence has been previously registered or resembles a registered trademark, whether under this Act or any previous company law, the first mentioned company, may by ordinary resolution and with the previous approval of the Central Government, signified in writing, change its name or new name.

The problem asked in the question is based upon the provision of Section 22(1) of the Companies Act, 1956. The new company registered under the name India Cosmetics Accessories Ltd. is identical in name with the existing India Cosmetics Limited. According to

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the aforesaid provisions of Section 22(1) the newly setup company should change its name. In such a case, the company can, on its own, change the name by obtaining previous approval of Central Government (new power delegated to Regional Director) and then by passing an ordinary resolution [Section 22(1)(a)] within 12 months of the registration. Such a change should be made within 3 months of the date of the direction of the Central Government being received or such longer period as the Central Government may deem fit to allow. The application for changing the name is required to be made to the Registrar of Companies in Form 1A with a fee of Rs. 500.

Where the name of a company has been changed the Registrar shall issue fresh certificate of incorporation with the changed name. Such change of name shall not affect any of the company's rights or obligations or affect any legal proceedings by or against it. Any legal proceedings which might have been continued or commenced by or against the company by its former name may be continued by its name under Section 23 of the Companies Act, 1956.

Question 12

The United Traders Association was constituted by two joint Hindu Families consisting of 21 major and 5 minor members. The Association was carrying on the business of trading as retailers with the object for acquisition of gains. The Association was not registered as a company under the Companies Act, 1956 or any other law.

State whether United Traders Association is having any legal status? Will there be any change in the status of this Association if the members of the United Traders Association subsequently were reduced to 15?
(November 2009)

Answer

Section 11 of the Companies Act, 1956 provides that no company, association or partnership consisting of more than 10 persons for the purpose of carrying on the business of banking and more than 20 persons for the purpose of carrying on any other business can be formed unless it is registered under the Companies Act or is formed in pursuance of some other Indian Law. Thus if such an association violates the provisions of Section 11 it is an "Illegal Association" although none of the objects for which it may have been formed is illegal.

This Section does not apply to a joint Hindu family but where the business is being carried on by two or more joint Hindu families the provisions of Section 11 shall be applicable. For computing the number of members for this purpose, minor members of such families shall be excluded.

Hence, the United Traders Association constituted by two joint Hindu Families is an Illegal Association according to the provisions of Section 11 as stated above.

Further such Association of more than 20 persons, if unregistered is invalid at its inception and cannot be validated by subsequent reduction in the number of members to below 20 (*Madan Lal vs. Janki Prasad 4 All 319*).

Unit – 2 : Prospectus

Question 13

ADJ Company Limited decides to buy-back its own shares. Advise the company's Board of Directors about the sources out of which the company can buy-back its own shares. What conditions are attached to the buy-back scheme of the company in accordance with the provisions of the Companies Act, 1956? Explain. (November 2007)

Answer

Buy-back of shares, sources and conditions (Section. 77A of the Companies Act, 1956):

In accordance with the provisions of the Companies Act, 1956, as contained in section. 77A, a company desirous of buy back of its own shares, can be advised to buy-back out of the following sources:

1. Company's free reserves; or
2. Company's securities premium Account; or
3. Out of the proceeds of any shared or other specified securities. [Section.77A(1)]. However, no buy-back of any kind of shares or other specified securities shall be made out of the proceeds of an earlier issue of the same kind of shares or same kind of other specified securities.

Conditions

- (1) Buy-back is authorised by the Company's Articles.
- (2) A special resolution has been passed in general meeting of the company authorising buy-back.
- (3) The buy-back is less than 25% of the total paid-up capital and free reserves of the company. The buy-back, however, cannot exceed 25% of company's paid up equity share capital in a financial year. Further the Companies (Amendment) Act 2001 (w.e.f. 23-10-2001) has authorised the buy back by passing a resolution of a meeting of the Board of Directors provided the buy back does not exceed 10% of the total paid up equity share capital and free reserves. However, there cannot be more than one such buy-back in any period of 365 days
- (4) The ratio of debt owed by the company is not more than two times the equity capital and free reserve after such buy back. However, the Central Government may prescribe a higher ratio of the debt for a class or classes of companies.
- (5) All shares or other specified securities are fully-paid-up,
- (6) The buy back with respect to listed securities is in accordance with the regulations made by the SEBI in this behalf.

Question 14

What is meant by 'Red-herring prospectus'? State the circumstances under which such prospectus is required to be filed with the Registrar of Companies. What is the requirement relating to filing of final prospectus in such cases? (May 2008)

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Answer

Red-herring Prospectus: What requirements of filing (Section 60-B of the Companies Act, 1956): Red-herring prospectus means a prospectus which does not have complete particulars on the price of securities and the quantum of securities offered [Explanation to Section 60B (4)]. A public company making an issue of securities may circulate information memorandum to the public prior to filing of prospectus [Section 60B (1)]. As per Section 2(19B), information memorandum means a process undertaken prior to the filing of prospectus by which a demand for the securities proposed to be issued by the company is elicited, and the price and terms of issue for such securities is assessed by means of notice, etc.

A company inviting subscription by an information memorandum shall be bound to file a prospectus prior to the opening of the subscription lists and the offer as red-herring prospectus, at least 3 days before the opening of offer [Section 60B (2)]. Exact issue size or issue price is not mentioned in the red-herring prospectus.

On the basis of offers received, company will finalise the issue price and issue size and then close the offer. After closure of offer of securities, a final prospectus will be prepared stating the total capital raised whether by way of debts, or share capital and the closing price of securities and any other details as were not complete in red-herring prospectus. The prospectus will be filled with ROC and also with SEBI in case of listed company. [Section 60B (9)].

Question 15

DJA Company Ltd., desirous of buying back of all its equity shares from the existing shareholders of the company, seeks your advice. Examining the provisions of the Companies Act, 1956 advise whether the above buy back of equity shares by the company is possible. Also state the sources out of which buy-back of shares can be financed. (May 2008)

Answer

Buy-back of Shares by Company (Section 77A of the Companies Act, 1956): The Company cannot buy back its entire equity shares from the existing shareholders. According to Section 77A of the Companies Act, 1956, buy back is restricted to 10% of its paid-up equity capital and free reserves authorised by the Board by means of a resolution passed at its meeting and upto 25% by way of a special resolution in a financial year. The sources out of which buy-back of shares can be finalised are:

- (a) Free reserves or
- (b) Security Premium account or
- (c) Proceeds of any shares or other specified securities.

Question 16

The Articles of Association of MSW Ltd. contained a provision that upto 4% of issue price of the shares may be paid as underwriting commission to the underwriters. The Board of directors decided to pay 5% underwriting commission. Can the Board of Directors do so? State the provisions of law in this regard as stated under the Companies Act, 1956. (November 2008)

Answer

According to the provisions of Section 76 (1) of the Companies Act, 1956 a company may pay a commission to any person who agrees to subscribe or procure subscription for an agreed number of shares or debentures of the company. Such commission may be paid to the underwriters who offer guarantee to procure applications for certain number of shares and guarantee to purchase the balance quantity of shares. For this, the underwriter gets underwriting commission. Maximum total commission payable cannot exceed 5% of the price of shares or the underwriter may be paid a lower rate if so prescribed by articles. In case of debentures it is 2½% or a lower rate if so prescribed in the articles.

In the given problem the articles of MSW Ltd has prescribed 4% underwriting commission but the directors decided to pay 5% underwriting commission. The directors cannot do so because under Section 76 (1) as aforesaid, such commission cannot be more than that prescribed in the Articles. Therefore the directors are not empowered to do so. Further, such amount of commission payable must be authorized by Articles. The agreed commission should be disclosed in the prospectus or the statement in lieu of prospectus. Copy of the contract for payment of commission must be filed with Registrar of companies at the time of the delivery of the prospectus or letter of offer [Section 76 (1)]. An underwriter must be also registered with SEBI.

Question 17

What is meant by “Shelf prospectus”? Who can file a “Shelf prospectus” with the Registrar of Companies? Stating the provisions of the Companies Act, 1956 point out the circumstances under which such prospectus is required to be filed with the Registrar of Companies.

(November 2008)

Answer

Section 60 A of the Companies Act, 1956 lays down the provisions as regards shelf prospectus. According to it, the shelf prospectus means a prospectus issued by any financial institution or bank for one or more issues of the securities or class of securities specified in that prospectus.

Therefore, any public financial institution, public sector bank or schedule bank whose main object is financing shall file a shelf prospectus. 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 the period of validity of such self prospectus.

A company filing a shelf prospectus shall be required to file an information memorandum on all material facts relating to charges created, and changes in the financial position as have occurred between the first offer of securities, previous offer of securities and the succeeding offer of securities within such time as may be prescribed by Central Government prior to making of a second or subsequent offer of securities under the shelf prospectus.

An information memorandum shall be filed along with such prospectus, which will remain valid for one year from the date of opening of the first issue of securities under that prospectus. Updated information memoranda filed with the shelf prospectus shall constitute the

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prospectus. Here financing means making loans or subscribing in the capital of a private industrial enterprise engaged in infrastructural financing or such other company which the Central Government may so notify in this behalf.

Question 18

What is meant by "Abridged Prospectus"? Is it necessary to furnish abridged form of prospectus along with the application form for shares? Under what circumstances an abridged prospectus need not accompany the detailed information regarding prospectus along with the application form?
(June 2009)

Answer

(1) Meaning of Abridged Prospectus:

According to Section 2(1) of the Companies Act, 1956, an abridged prospectus means memorandum containing such salient features of a prospectus as may be prescribed. The memorandum containing salient features of the prospectus accompanying the application forms shall be as per rules prescribed by the Central Government in this behalf. It is however, open to a company to attach full prospectus along with the application forms.

(2) Abridged prospectus to be issued along with application form:

A company can not issue application forms for shares or debentures unless the form is accompanied by abridged prospectus, according to Section 56(3) of the Companies Act, 1956. The abridged prospectus and application form should bear the same printed number. The investor may detach the share application form along the perforated line, after he has had an opportunity to study the contents of this abridged prospectus. The objective of this provision is to reduce the cost of issue as the detailed prospectus is a very bulky document whereas the contents of abridged prospectus are limited. Penalty for failure to comply with Section 56(3) can be a fine of up to Rs.50, 000.

(3) Circumstances under which the abridged prospectus containing all the prescribed details need not accompany the application forms:

An abridged prospectus containing all the prescribed details need not accompany the application form in the following circumstances:

- (i) In case of bona fide underwriting agreement [Section 56(3)(a)]
- (ii) Where shares and debentures are not issued to the public [Section 56(3)(b)].
- (iii) where the offer is made only to existing members or debenture holders of the company [Section 56(5)(a)].
- (iv) In case of issue of shares or debentures which are in all respect similar to those previously issued and dealt in a recognized stock exchange [Section 56(5)(b)].

Question 19

Modern Furnitures Limited was willing to purchase teakwood estate in Chhattisgarh State. Its prospectus contained some important extracts from an expert report giving the number of

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teakwood trees and other relevant information in the estate in Chhattisgarh State. The report was found inaccurate. Mr. 'X' purchased the shares of Modern Furnitures Limited on the basis of the above statement in the prospectus. Will Mr. 'X' have any remedy against the company? When will an expert not be liable? State the provisions of the Companies Act, 1956 in this respect.
(November 2009)

Answer

In the event of any mis-statement in a prospectus, the allottees have certain remedies against the company as well as against those who were responsible for the issue of such a prospectus. Thus, in the present case the allottee Mr. X shall have the right to claim compensation from Modern Furnitures Ltd., for any loss that he might have sustained in terms of the value of shares. But his claim against those responsible for issue of prospectus shall not succeed since they made the statement on the basis of the report of an expert whom they believed to be competent. Section 62(2) of the Companies Act, 1956 provides that in such circumstances, one shall not incur liability. However, the expert can be proceeded against, for the inaccurate report which he had made.

An expert shall not be liable if he proves:

- (i) that having given his consent, he withdrew it in writing before delivery of the copy of prospectus for registration or
- (ii) that after delivery of prospectus for registration and before allotment he became aware of the untrue statement and withdrew his consent in writing and gave reasonable public notice of the withdrawal and his reasons therefor; or
- (iii) that he was competent to make the statement and believed on reasonable grounds that it was true.

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Unit – 3 : Share Capital

Question 20

Explain in brief 'Equity Share Capital' and 'Preference Share Capital'. (May 2007)

Answer

As per the Section 85 and 86 of the Companies Act 1956, there will now be two types of share capital as under:

Share Capital:

The share capital of a company limited by shares shall be of two kinds only, namely –

- (i) equity share capital and
- (ii) preferential share capital.

Equity Share Capital shall be:

- (i) with voting rights
- (ii) with differential rights. The expression 'Shares with differential voting rights' is defined as a share that is issued in accordance with the provisions of Section 86.

Equity shares carry voting rights on the ground meetings of the company and have the right to control the management of the company. They have right to share in the profits of the company in the form of distribution of dividend and bonus shares. In the event of winding up of the company, equity shares capital is repayable only after repayment of the claims of the creditors and preference share capital.

Preference share capital means that part of share capital which fulfils both the following requirements, namely

- (a) as respect dividend, it carries or will carry a preferential right to be paid a fixed amount or an amount calculated at a fixed rate, and
- (b) as respect capital, it carries or will carry on the winding up or repayment of capital, a preferential right to be repaid the amount of the capital paid up or deemed to have been paid up, whether or not there is a preferential right to the payment of either or both of the following amounts, namely –
 - (i) any money remaining unpaid, in respect of the amount specified in clause (a), upto the date of winding up or repayment of capital; and
 - (ii) any fixed premium any fixed scale, specified in the memorandum or articles of the company (Section 85).

Question 21

A Public Company proposes to issue 'Sweet Equity Shares' to its employees. Referring to the provisions of the Companies Act, 1956, state the conditions required to be fulfilled by the Company. (May 2008)

Answer

Sweat Equity Shares: Conditions (Section 79A of the Companies Act, 1956)

Sweat Equity Shares may be issued by a public company if the following conditions are fulfilled as contained in Section 79A of the Companies Act, 1956.

1. Shares of a class which have already been issued only can be issued as sweat equity shares.
2. The issue of sweat equity shares should be authorized by a special resolution by the company in general meeting. The resolution should specify number of shares, current market price, consideration, if any, and class or classes of directors or employee to whom the 'sweat equity shares' may be issued.
3. The sweat equity shares can be issued only one year after the company was entitled to commence business.
4. If the company is listed on the stock exchange, sweat equity shares can be issued as per regulation made by SEBI. In the case of unlisted companies, sweat equity shares will be issued in accordance with guidelines which may be prescribed by the Central Government.
5. The 'Sweat Equity Shares' have same limitations, restrictions and rights as are applicable to other equity shares.

Question 22

A charge requiring registration with Registrar of Companies was created on 1st February, 2008 by XYZ Limited. The Secretary of the Company realised on 15th March, 2008 that the charge was not filed with the Registrar. State the steps to be taken by the Secretary to get the charge registered with the Registrar.
(May 2008)

Answer

Registration of Charge: Steps for belated registration (Section 125 of the Companies Act, 1956): A charge should be registered within 30 days after the date of its creation. In this case the charge was created on 1st Feb, 2008. Hence the particulars of charge are required to be filed with the Registrar on or before 2nd March, 2008 [Section 125 (1)]. The Secretary of the company realised only on 15th March, 2008 that the charge was not filed with the Registrar. It is, however, open to the Registrar to allow the particulars of the charge to be filed within 30 days next following the expiry of the period of 30 days if the company satisfies the Registrar that it had sufficient cause for not filling the particulars within 30 days. [Proviso to Section 125(1)]. The Secretary may take advantage of this provision and immediately file the particulars of charge with the Registrar giving adequate reasons for the delay. If the Registrar is satisfied, he may allow registration on payment of additional fee.

Question 23

While sanctioning working limit, the rate of interest had been fixed at a specified percentage above the bank rate as notified by the Reserve Bank of India. There was a change in the

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interest rate due to Reserve Bank of India notification issued later. The Bank insisted on filing a return of modification of charges. Is the stand of the bank correct? Discuss in the light of the provisions of the Companies Act, 1956. (June 2009)

Answer

Section 135 of the Companies Act, 1956 provides that “whenever the terms or conditions or the extent or operation of any charge registered under this part are or is modified, it shall be the duty of the company to send to the Registrar the particulars of such modifications and the provisions of this part as to registration of a charge shall apply to modification of the charge.”

Here the term modification includes variation of any terms of the agreement including variation of rate of interest (other than bank rate), which may be by mutual agreement or by operation of law. In the light of the above, the change in the rate of interest constitutes modification. Therefore the stand of the bank is correct.

Question 24

Mr. 'Y', the transferee, acquired 250 equity shares of BRS Limited from Mr. 'X', the transferor. But the signature of Mr. 'X', the transferor, on the transfer deed was forged. Mr. 'Y' after getting the shares registered by the company in his name, sold 150 equity shares to Mr. 'Z' on the basis of the share certificate issued by BRS Limited. Mr. 'Y' and 'Z' were not aware of the forgery. State the rights of Mr. 'X', 'Y' and 'Z' against the company with reference to the aforesaid shares. (November 2009)

Answer

According to Section 84(1) of the Companies Act, 1956, a share certificate once issued amounts to a declaration by the company to all the world that the person in whose name the certificate is made out and to whom it is given is a share holder in the company; in other words, the company is estopped from denying his title to the shares. However, a forged transfer is a nullity. It does not give the transferee (Y) any title to the shares. If the company acts on a forged transfer and removes the name of the real owner (X) from the Register of Members, then the company is bound to restore the name of X 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).

In the above case, 'Z' being the bona fide purchaser must be compensated by the company. 'Z' shall have therefore a right to claim the market price of those shares at that time. However 'Z' cannot insist on being placed on the register of members to which 'X' alone is eligible as he cannot be said to have consented to the transfer. 'Y' shall of course be liable to the company to indemnify the loss on account of payment to 'Z'. A similar decision was given in *Dixon v. Kennaway*.

Unit – 4 : Meetings

Question 25

What is E filing? List at least five advantages of E filing under MCA 21. (May 2007)

Answer

The term E-filing indicates the process of getting services electronically with a comprehensive on-line portal. The advantages are:

1. Instant registration of companies;
2. Simplified and more facile method of filing documents;
3. Total transparency;
4. Easier and better compliance of regulations;
5. Utmost customer care
6. Authentic and reliable filling of forms / returns through professionals;
7. Centralised database management;
8. Better service availability;
9. Filing of and inspection of documents anywhere and anytime;
10. Quick redressal of investor grievances;
11. Supervisor and monitoring of compliance made easier;

Question 26

The quorum for a General meeting of a public company is 15 members personally present according to the provisions of the Articles of Association of the company. Examine with reference to the provisions of the Companies Act, 1956 whether there is proper quorum at a General Meeting of the company which was attended by the following persons:

- (i) 13 members personally present
- (ii) 2 members represented by proxies who are not members of the company
- (iii) One person representing two member companies. (November 2007)

Answer

Quorum: According to section 174 of the Companies Act, 1956 unless the Articles of the company provide for a larger number, 5 members personally present in the case of a public company shall be the quorum for a meeting of the company.

In this case articles of the company provide for a larger number of 15, hence the quorum is 15.

The words 'personally present' exclude proxies. Hence two members represented by proxies cannot be counted for the purpose of quorum. However, the representative of a body corporate appointed under section 187 is a member 'personally present' for the purpose of counting a quorum. In case two or more corporate bodies who are members of the company

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are represented by single individual each of the bodies corporate will be treated as personally present by the individual representing it. In this case one person represent two member companies and his presence will be counted as two members being present in person for the purpose of quorum. Hence 15 members are personally present (13+2) and as such there is proper quorum.

Question 27

Developers Ltd. hold a General Meeting of shareholders for passing a special resolution regarding alteration of Articles of Association. Out of the members present in the meeting 20 voted in favour, 4 against and 8 members did not vote and remained absent from voting. The Chairman of the meeting declared the resolution as passed. Is it a valid resolution as per the provisions of the Companies Act, 1956 ?
(November 2008)

Answer

In accordance with Section 189 (2) of the Companies Act, 1956 the votes cast in favour of a resolution (whether by show of hands or in a poll as the case may be) by members who, being entitled so to do, vote in person or where proxies are allowed, by proxy, are not less than three times the number of votes if any, cast against the resolution by members so entitled and voting is called special resolution.

Hence in accordance with the above mentioned provisions, the resolution passed in the general meeting of the Developers Ltd, is a valid resolution since the vote cast in favour of the resolution are more than 3 times the number of votes cast against the resolution.

Question 28

Annual General Meeting of MGR Limited is convened on 28th December, 2008. Mr. J, who is a member of the company, approaches the company on 28th December, 2008 and demands inspection of proxies lodged with the company. Explain the legal position as stated under the Companies Act, 1956 in this regard.
(June 2009)

Answer

Every member entitled to vote at a meeting of the company or on any resolution to be moved thereat, shall be entitled during the period beginning 24 hours before the time fixed for the commencement of the meeting and ending with the conclusion of the meeting, to inspect the proxies lodged, at anytime during the business hours of the company. Provided not less than 3 days' notice in writing of the intention to inspect is given to the company [Section 176(7) of the Companies Act, 1956].

In the given case, Mr. J who is a member approaches the company on 28th December and demands inspection of proxies lodged with the company. Based on the above provisions since prior notice had not been given by Mr. J to the company for inspecting the proxies, the company may refuse inspection of proxy forms.

Question 29

M. H. Company Limited served a notice of general meeting upon its shareholders. The notice stated that the issue of sweat equity shares would be considered at such meeting. Mr. 'A', a shareholder of the M. H. Company Limited complains that the issue of sweat equity shares was not specified fully in the notice. Is the notice issued by M. H. Company Limited regarding issue of sweat equity shares valid according to the provisions of the Companies Act, 1956? Explain in detail.
(November 2009)

Answer

Section 173 of the Companies Act, 1956 requires a company to annex an explanatory statement to every notice for a meeting of the company at which some special business is to be transacted. This explanatory statement is to bring to the notice of members all material facts relating to each item of special business. Section 173 further specifies that all business in case of any meeting other than (i) consideration and approval of the annual accounts of the company (ii) declaration of dividend (iii) appointment of directors in place of those retiring and (iv) appointment of auditors including the fixing of their remuneration is regarded as special business. Therefore, the complaint of Mr. A, the shareholder is valid, since the details on the item regarding issue of sweat equity shares to be considered is lacking. The information about the issue of sweat equity shares is a material fact. The notice given by M. H. Ltd. of the General Meeting of the shareholders is not a valid notice under Section 173 of the Companies Act, 1956.

NOTE

[illegible]