

EXECUTIVE PROGRAMME

DECEMBER 2009

COMPANY LAW

Time allowed : 3 hours

Maximum marks : 100

NOTE : 1. Answer **SIX** questions including Question No. 1 which is **COMPULSORY**.

2. All references to sections relate to the Companies Act, 1956 unless stated otherwise.

Question 1

Attempt any four of the following :

- (i) *"Some definite criteria will have to be fulfilled to identify a corporation as State within the meaning of Article 12 of the Constitution of India." Comment.*
- (ii) *"Diminution of share capital is not always regarded as reduction of capital." Comment.*
- (iii) *"A limited company will have to get certain resolutions passed only through postal ballot instead of transacting the business in the general meeting of the company." Discuss.*
- (iv) *"Oppression need not be continuous." Discuss.*
- (v) *"Common seal of a company will have to be affixed on all the letters and documents of the company." Discuss. (5 marks each)*

Answer 1(i)

When an association of persons is incorporated according to the law of land and is clothed with legal personality, it becomes a legal entity, separate from the persons constituting it. It is then known as corporation.

A company formed under an Act of Parliament or State Legislature is called a statutory corporation.

The statutory character of the corporation identifies a corporation as STATE within the meaning of Article 12 of the Constitution of India.

The relevant criteria according to the judgement delivered by Bhagwati J. in the case of *Raman Dayaram Shetty v. International Airport Authority*, AIR 1979 S.C. 1628 and later accepted in other cases including the case of *Som Prakash v. Union of India* AIR 1981 SC 212 are –

- (1) the source of the share capital;
- (2) the extent of State control over corporation and whether it is deep and pervasive;
- (3) whether the corporation has monopoly status;
- (4) whether functions of the corporation are of public importance and closely related to Governmental functions; and
- (5) whether what belonged to a department of government formerly was transferred to the corporation.

Answer 1(ii)

Reduction of capital involves writing off past losses against capital, cancellation of the uncalled capital or repayment of surplus capital. It may involve reduction of issued, subscribed or paid up share capital of the company. Diminution of capital under Section 94 does not constitute a reduction of capital within the meaning of the Companies Act.

In the following cases, the diminution of share capital is not to be treated as reduction of share capital:

- (i) when a company cancels shares not taken and/or agreed to be taken by any person [section 94(1)(e)];
- (ii) when redeemable preference shares are redeemed;
- (iii) where any share is forfeited for non-payment of calls;
- (iv) where the company buy back its own share under section 77A of the Act.

In all these cases, the procedure for reduction of capital as laid down in Section 100 is not attracted.

Answer 1(iii)

As per Companies (Passing of the Resolution by Postal Ballot) Rules, 2001, a certain resolutions will have to be passed only through Postal Ballot.

List of businesses in which the resolutions shall be passed only through Postal Ballot are:

- (i) alteration of the object of Memorandum;
- (ii) alteration of the Articles of Association in relation to deletion or insertion of provisions defining private company;
- (iii) buy back of own share;
- (iv) issue of shares with differential voting rights;
- (v) change of place of the registered office outside the local limits of the city, town, village;
- (vi) sale of whole or substantially whole of the undertaking of the company;
- (vii) giving loan or extending guarantee, or providing security in excess of the limit provided under section 372A.
- (viii) election of a director under the proviso to sub-section (1) of section 252 of the Act;
- (ix) variation of rights attached to a class of shares or debenture or other securities as specified under section 106.

Answer 1(iv)

“Oppression must be a continuous process. This is suggested by the words, ‘are being conducted in a manner...’ used in Section 397. Hence isolated acts of oppression or mismanagement will not give rise to an action under Section 397 of the Act. In Shanti

Pd. Jain's Case, the court said: "events have to be considered not in isolation but as a part of a consecutive story. There must be continuous acts on the part of the majority shareholders, continuing up-to-date of petition."

In *Ramshankar Prasad v. Sindu Iron Foundry (P) Ltd.*, AIR 1966 Cal 512, it was held that a petition under Section 397, would be maintainable even if the oppression was of a short duration and of a singular conduct if its effects persisted indefinitely [followed in *Maharashtra Power Development Corpn. Ltd. v. Dabhol Power Co. Ltd.* (2003) 56 CLA 263 (Bom.)].

Answer 1(v)

The statement, "Common seal of a company will have to be affixed on all the letters and documents of the company" is not correct.

Statutorily, the common seal is required to be affixed to the following documents:

- Power of attorney empowering any person as the company's attorney to execute deeds in or outside India. [section 48 (1)]
- Documents authorizing any person in a territory outside India to affix the company's official seal to a deed or other documents. [section 50 (2)]
- Share certificates. (section 84)
- Share warrant. (section 114)

Thus, other documents need not be under the common seal [section 54], except to the extent provided in the articles of association. Further, it is not statutorily required that debenture certificates should be issued under the common seal.

The company's seal may, however, be affixed to various deeds and agreements like lease deed, sale deed, debenture trust deeds, promissory notes, negotiable instruments (except cheques), hypothecation, loan agreements, guarantees, etc.

Question 2

(a) Choose the most appropriate answer from the given options in respect of the following :

- (i) Out of the following statements, which one is correct with regard to listing of securities —
 - (a) The shares and debentures of a public company may be quoted on a stock exchange
 - (b) The shares and debentures of a private company may be quoted on a stock exchange
 - (c) Only the shares and not the debentures of a public company may be quoted on a stock exchange
 - (d) Only the shares and not the debentures of a private company may be quoted on a stock exchange.
- (ii) Sweat equity shares issued to employees or directors of a company shall be locked-in for a period of —
 - (a) Three years from the date of allotment

- (b) *Two years from the date of allotment*
- (c) *Five years from the date of allotment*
- (d) *Twelve months from the date of allotment.*
- (iii) *The companies which need not have their own articles of association are —*
 - (a) *Unlimited companies*
 - (b) *Companies limited by guarantee*
 - (c) *Private companies limited by shares*
 - (d) *Public companies limited by shares.*
- (iv) *According to the SEBI Guidelines, the issue of bonus shares should be made within a period of —*
 - (a) *Three months from the date of approval of the Board of directors*
 - (b) *Six months from the date of approval of the Board of directors*
 - (c) *Twelve months from the date of approval of the Board of directors*
 - (d) *Thirty days from the date of approval of the Board of directors.*
- (v) *Out of the following statements, which one is incorrect as regard to the Director Identification Number (DIN) —*
 - (a) *DIN is a unique identification number and once obtained is valid throughout the lifetime of a director*
 - (b) *DIN is mandatory for all directors of Indian companies whether they are citizens of India or not*
 - (c) *DIN is mandatory for directors of foreign company having branch offices in India*
 - (d) *A single DIN is required for an individual irrespective of number of directorships held by him.* (1 mark each)
- (b) *Re-write the following sentences after filling-in the blank spaces with appropriate word(s)/figure(s) :*
 - (i) *In case of listed companies, where the shares are transferable through electronic mode, transfers are made through _____ instead of physical transfers.*
 - (ii) *The voting power of a guarantee company having share capital is determined by the _____ and not by the guarantee.*
 - (iii) *_____ is the total of the called-up capital remaining unpaid.*
 - (iv) *No person shall hold office at the same time as small shareholders' director in more than _____ companies.*
 - (v) *_____ includes a reorganisation of share capital of company by consolidation of shares of different classes or division of shares into shares of different classes or by both these methods.* (1 mark each)
- (c) *State the salient features of a 'limited liability partnership' (LLP). (6 marks)*

Answer 2(a)(i)

- (a) The shares and debentures of a public company may be quoted on a Stock Exchange.

Answer 2(a)(ii)

- (a) Three years from the date of allotment.

Answer 2(a)(iii)

- (d) Public companies limited by shares.

Answer 2(a)(iv)

- (b) Six months from the date of approval of the Board of directors.

Answer 2(a)(v)

- (c) DIN is mandatory for directors of foreign company having branch offices in India.

Answer 2(b)

- (i) In case of listed companies, where the shares are transferable through electronic mode, transfers are made through **Depository Participants** instead of physical transfers.
- (ii) The voting power of a guarantee company having share capital is determined by the **shareholding** and not by the guarantee.
- (iii) **Unpaid capital** is the total of the called-up capital remaining unpaid.
- (iv) No person shall hold office at the same time as small shareholders' director in more than **two** companies.
- (v) **Arrangement** includes a reorganisation of share capital of company by consolidation of shares of different classes or division of shares into shares of different classes or by both these methods.

Answer 2(c)

The salient features of the Limited Liability Partnership are as follows:—

- (i) The LLP is a body corporate and a legal entity separate from its partners. Any two or more persons, associated for carrying on a lawful business with a view to profit, may by subscribing their names to an incorporation document and filing the same with the Registrar, form a Limited Liability Partnership. The LLP has a perpetual succession;
- (ii) The mutual rights and duties of partners of an LLP inter se and those of the LLP and its partners shall be governed by an agreement between partners or between the LLP and the partners subject to the provisions of the proposed legislation. There would be flexibility to devise the agreement as per their choice. In the absence of any such agreement, the mutual rights and duties shall be governed by the provisions of the proposed legislation;

- (iii) A LLP is a separate legal entity, liable to the full extent of its assets, with the liability of the partners being limited to their agreed contribution in the LLP which may be tangible or intangible in nature or both tangible and intangible in nature. No partner would be liable on account of the independent or un-authorized acts of other partners or their misconduct;
- (iv) Every LLP shall have at least two partners and shall also have at least two individuals as Designated Partners, of whom at least one shall be resident in India. The duties and obligations of Designated Partners shall be as provided in the law;
- (v) The LLP shall be under an obligation to maintain annual accounts reflecting true and fair view of its state of affairs. A statement of accounts and solvency shall be filed by every LLP with the Registrar every year. The accounts of LLPs shall also be audited, subject to any class of LLPs being exempted from this requirement by the Central Government;
- (vi) The Central Government shall have powers to investigate the affairs of an LLP, if required, by appointment of competent inspector for the purpose;
- (vii) The proposed legislation would confer powers on the Central Government to apply such provisions of the Companies Act, 1956 to provide, inter alia, for mergers, amalgamations, winding up and dissolutions of LLPs, as appropriate, by notification with such changes or modifications as deemed necessary. However, such notifications shall be laid in draft before each House of Parliament for a total period of 30 days and shall be subject to any modification as may be approved by both Houses;
- (viii) The Indian Partnership Act, 1932 shall not be applicable to LLPs. Other entities may convert themselves to LLP in accordance with provisions of the proposed legislation;
- (ix) The Central Government shall have powers to make rules for carrying out the provisions of the proposed legislation.

Question 3

Distinguish between any four of the following :

- (i) *'Reserve capital' and 'capital reserve'.*
- (ii) *'Sweat equity' and 'issue of capital on preferential basis'.*
- (iii) *'ESOS' and 'ESPS'.*
- (iv) *'Motion' and 'resolution'.*
- (v) *'Shelf prospectus' and 'red-herring prospectus'.* (4 marks each)

Answer 3(i)

Reserve capital is that part of uncalled capital of a company which the limited company has decided by special resolution in terms of section 99 of the Act, not to call except in the event of or for the purpose of the company being wound up. Hence, Reserve capital is that part of the uncalled share capital which may be called up on happening of that event or at the time of winding up.

For instance, against a share of face value of Rs.10 only Rs.5 has been paid up. Out of Rs.5 uncalled capital, by passing special resolutions Rs.2 has been kept as Reserve capital which may be called up on happening of certain events or at the time of winding up. Rs.2 is reserve capital per share.

Reserve capital is distinct from capital reserve since the latter is created out of profit while reserve capital is part of uncalled share capital.

Capital reserve is created out of capital profits or earnings which are not ordinarily distributable among shareholders of the company. The Capital Reserve has the securities premium, capital redemption revaluation of assets etc.

Answer 3(ii)

Sweat equity shares means equity shares issued by a company to its employees or directors at a discount or for consideration, other than cash for providing know how or making available a right in the nature of intellectual property rights or value additions, by whatever name called.

A company can issue sweat equity shares of or class of shares already issued with the approval of the members by special resolution clearly specifying therein the number of shares being issued, current market price, consideration if any, class or classes of directors or employees to which such sweat equity shares have been proposed to be issued.

Issue of capital on preferential basis by way of equity shares/FCDs/PCDs or any other financial instruments shall comply with the requirements of Chapter XIII of SEBI (DIP) Guidelines, 2000. Such issues are made to any selected group of persons. The offer prices of the shares should not be less than the higher of the average of the weekly high and low of the closing price of related shares quoted in the stock exchange during the six months or two weeks preceding the relevant date.

Answer 3(iii)

ESOS or Employee Stock Option Scheme means a scheme under which options given to the whole-time directors, officers or employees of a company to purchase or subscribe at a future date, the securities offered by the company at a predetermined price.

No ESOS can be offered to the employees of the company unless the shareholders of the company approve ESOS by passing special resolution in the general meeting.

The company shall have freedom to specify the lock-in-period for the shares issued on exercise of option.

ESPS or employee stock purchase scheme means a scheme under which the company offers shares to employees as part of a public issue or otherwise.

An employee who is a promoter or belongs to a group of promoters shall not be eligible to participate in ESPS.

Issue of ESPS requires approval of the shareholders of the company by passing special resolution in the general body meeting of the shareholders.

ESPS will have lock-in period of minimum one year.

Answer 3(iv)

Motion is a proposal submitted in a meeting for discussion. A motion should be in writing and signed by the mover and put to vote at the meeting by the chairman.

Motion becomes a resolution only after the requisite majority of members have adopted it. Resolutions are of three types (a) ordinary, (b) special and (c) resolutions requiring special notice. Certain resolutions are required to be passed by postal ballot. Certain resolutions are required to be filed with the Registrar within 30 days of the meeting in which the resolutions are passed.

Answer 3(v)

Shelf Prospectus – According to section 60A of the Act –

- (1) Any public financial institution, public sector bank or scheduled bank whose main object is financing shall file a shelf prospectus.
- (2) A company (financial institutions, banks) 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 one year from the date of opening of the first issue of securities.
- (3) A company filing shelf prospectus shall be required to file an information memorandum of all material facts relating to new charges created, changes in the financial position, etc.
- (4) An information memorandum shall be issued to public along with shelf prospectus filed at the stage of first offer of securities. Such prospectus will remain valid for one year.

The concept of shelf prospectus is to save expenditure on issue of fresh prospectus every time within a period of one year.

Red-herring prospectus on the other hand means a prospectus which does not have complete particulars on the price of the securities offered and the quantum of securities offered. The information memorandum and red-herring prospectus carry same obligations as are applicable in the case of prospectus. Every variation between the information memorandum and the red-herring prospectus shall be highlighted by the issuer company and shall be individually intimated to the persons invited to subscribe the securities.

Question 4

- (a) *Define 'prospectus'. What are the ingredients to constitute a prospectus*
(6 marks)
- (b) *What are the documents required to be attached with the draft red-herring prospectus to be filed with the Registrar of Companies ?*
(6 marks)
- (c) *Registrar of Companies can refuse registration of prospectus. Explain.*
(4 marks)

Answer 4(a)

Section 2(36) defines a prospectus as “any document described or issued as a prospectus and includes any notice, circular, advertisement or other document inviting

deposits from the public or inviting offers from the public for the subscription or purchase of any shares in, or debentures of a body corporate.”

The following ingredients may be said to constitute a ‘prospectus’:

- (a) there must be an invitation to the public;
- (b) the invitation must be made “by or on behalf of the company or in relation to an intended company”;
- (c) the invitation must be “to subscribe or purchase”;
- (d) the invitation must relate to shares or debentures or such other instrument.

In essence, it means that a prospectus is an invitation issued to the public to offer for purchase/subscribe shares or debentures of the company (*Immugan v. Ranga Ram*, A.I.R. 1934 Mad. 641). Any advertisement offering shares or debentures of the company for sale to the public is a prospectus.

Answer 4(b)

The following documents must be attached to the copy of a draft red-herring prospectus filed with the Registrar:

- (i) the consent of the expert mentioned in the prospectus;
- (ii) a copy of every contract relating to the appointment or remuneration of a managing director or manager;
- (iii) a copy of every material contract not being a contract entered into in the ordinary course of business of the company entered into within two years of the issue of prospectus;
- (iv) a written statement relating to the adjustments, if any, in respect of figures of any profits or losses, and assets and liabilities;
- (v) the consent in writing of the person, if any, named in the prospectus as the auditor, legal adviser, attorney, solicitor, issue house, banker, manager to the issue, or broker of the company to act in that capacity;
- (vi) the consent of the director under section 266 in respect of new directors, if any, named therein;
- (vii) a copy of the underwriting agreement, if any.

Answer 4(c)

The Registrar shall not register a prospectus if –

- (i) it is not dated;
- (ii) it does not comply with the requirements of section 56 as to the matters and reports to be set out in it;
- (iii) it contains statement of experts connected with the formation, promotion or management of the company;

- (iv) it does not contain a statement from expert stating that he has given and has not withdrawn his consent for inclusion of his name;
- (v) it does not contain consent of the director or auditor, legal advisers, attorney, solicitor, issue house, banker, managers to the issue, broker named in the prospectus to act as such.

Question 5

- (a) *State, with reasons in brief, whether the following statements are correct or incorrect:*
- (i) *A company, being a body corporate, can sue and be sued in its own name.*
 - (ii) *A government company is neither a government department nor a government establishment.*
 - (iii) *Under section 14, the memorandum of association of a company may be in any form.*
 - (iv) *A director is liable for acts of his co-directors.*
 - (v) *Every shareholder has the right of nomination of shares. (2 marks each)*
- (b) *Tuff Ltd. is a public limited company, which was registered in the year 1991 under the Companies Act, 1956. After eighteen years of existence as a public company, the said company now wants to convert itself into a private limited company. Is it possible ? If yes, explain the legal requirements, if any.*
- (6 marks)

Answer 5(a)(i)**Correct.**

A company being a body corporate can sue and be sued in its own name. 'To sue' means to institute legal proceedings against (a person) or to bring a suit in a court of law. All legal proceedings against the company are to be instituted in its own name. Similarly, the company may bring an action against anyone in its own name. A company, as a person separate from its members, may even sue one of its own members for libel.

Answer 5(a)(ii)**Correct.**

In *Hindustan Steel Works Construction Ltd. v. State of Kerala* [1998] 2 Comp CLJ 383, it was held that in spite of all the control of the Government, a government company is neither a government department nor a Government establishment, it is just an agency of the Government. Similarly, the employees of a Government Company are not the employees of the Central or State Government.

Answer 5(a)(iii)**Incorrect.**

Section 14 of the Companies Act provides that the memorandum of association should be in any one of the Forms specified in Tables B, C, D and E of Schedule I of the Companies Act, 1956, as may be applicable in relation to the type of company proposed to be incorporated or in a Form as near thereto as the circumstances admit.

Answer 5(a)(iv)**Incorrect.**

A director is an agent of the company and not of other members of the Board. Anything done by the Board cannot make a director liable who did not know that action and did not participate in it, even if he attends the subsequent meeting at which the minutes recording the wrongful action of the earlier meeting are confirmed. A director could not be liable for the misconduct of another director unless he has joined with him in the perpetration of the wrong or has omitted to thwart the wrong due to his negligence [*Life Insurance Corporation v. Haridas Mundra* (1966) 26 Com. Cases 371 (D.B)(All)]. In the absence of reasonable grounds for suspicion, a director cannot be held liable for the fraudulent acts of co-director on the ground that he ought to have discovered the fraud [*Dovey v. Cory* (1901) A.C.477].

Answer 5(a)(v)**Incorrect.**

Only individuals who are applying/holding shares or debentures on their own behalf singly or jointly can make the nomination. In other words, non-individuals including society, trust, body corporate, partnership firms, Karta of Hindu Undivided Family, holder of power of attorney cannot nominate.

Answer 5(b)

A public company can be converted into a private company only after the approval of the Central Government. It cannot be treated as a private company till the Central Government accords its approval. Conversion of a public company into a private company will require:

- Passing of a special resolution authorizing the conversion and altering the Articles so as to include the matters specified in section 3(1)(iii).
- Changing the name of the company by special resolution as required by section 21.
- Obtaining the approval of the Central Government as required by section 31. Proviso to section 31(1) provides that no alteration made in the Articles, which has the effect of converting a public company, shall have effect unless such alteration has been approved by the Central Government.
- Filing of printed copy of the articles as altered within one month of the receipt of the approval of the Central Government with the Registrar of Companies.

Therefore, Tuff Ltd. can be converted into a private company even after eighteen years of existence as a public company provided it complies with the procedure as mentioned above.

Question 6

- (a) *The power to invest funds of the company is the prerogative of the Board of directors under section 292. Discuss the limitations on such powers of the Board, if any, relating to inter-corporate loans and investments under section 372A.* (6 marks)

- (b) *With the approval of the Board, an amount of Rs.50 crore was spent by Speed Jet Ltd., in producing a commercial film, not covered under its objects clause. The film was a complete flop and the company lost an amount of Rs.40 crore. Some of the members of the company objected to such investments not covered by the objects clause of the company. They filed a suit in the court of law making the directors personally responsible and to make good the loss. Will they succeed ? Support your answer with reasons. (6 marks)*
- (c) *What is meant by 'doctrine of ultra vires' ? (4 marks)*

Answer 6(a)

Subject to limitations under different sections of the Act and limitations under the Memorandum and Articles of Associations of the company, section 292 of the Companies Act, 1956 has given wide powers to the Board of Directors of a company to invest the funds of the company. Every resolution of the Board delegating the powers must specify the total amount up to which the funds of the company may be invested and the nature of the investment which may be made by the delegate under clause (d) of section 292(1). [Section 292(3)].

Moreover, the Board also has the power to make loans, borrow money etc. Board's power under section 292 to make loans, give guarantee or provide security has been restricted under section 372A of the Act.

As per Section 372A :

No Company shall, directly or indirectly:

- (a) make any loan to any other body corporate;
- (b) give any guarantee, or provide security, in connection with a loan made by any other person to, or to any other person by, any body corporate; and
- (c) acquire, by way of subscription, purchase or otherwise the securities of any other body corporate;

exceeding 60% of its paid-up share capital and free reserves, whichever is more.

However, a company may make loan, give any guarantee or provide security and/or make investment in aggregate exceeding the aforesaid limits of 60% or 100% if the same is previously authorized by a special resolution passed in a general meeting.

Answer 6(b)

In the case of a company whatever is not stated in the memorandum as the objects or powers is prohibited by the doctrine of ultra vires. As a result, an act which is ultra vires is void, and does not bind the company. Neither the company nor the other contracting party can sue on it. Also, as stated earlier, the company cannot make it valid, even if every member assents to it.

Further, it is one of the duties of directors to ensure that the corporate capital is used only for the legitimate business of the company and hence if such capital is diverted to purposes foreign to company's memorandum, the director will be personally liable to replace it. In *Jehangir R. Modi v. Shamji Ladha*, [(1866-67) 4 Bom. HCR (1855)], the Bombay High Court held: "A shareholder can maintain an action against the directors to compel them to restore to the company the funds of the company that have by them

been employed in transactions that they have no authority to enter into, without making the company a party to the suit”.

In the present case, the company Speed Jet Ltd. invested an amount of Rs.50 crores in producing a commercial film not covered under the object clause of the company. The act of the company is ultra vires and the persons responsible for entering into the venture are personally responsible for the loss of the company. They are liable to make good the loss thereof to the company.

The suit filed in the court is tenable.

Answer 6(c)

Doctrine of *Ultra Vires*

The word ‘ultra’ means beyond and the word ‘vires’ means the powers. So, the meaning of the word ultra vires means beyond the power. In the case of a company whatever is not stated in the memorandum as the objects or powers is prohibited by the doctrine of *ultra vires*. As a result, an act which is *ultra vires* is void, and does not bind the company. Neither the company nor the other contracting party can sue on it. The company cannot make it valid, even if every member assents to it.

The general rule is that an act which is ultra vires the company is incapable of ratification. An act which is intra vires the company but outside the authority of the directors may be ratified by the company in proper form [*Rajendra Nath Dutta v. Shilendra Nath Mukherjee*, (1982) 52 Comp. Cas. 293 (Cal.)].

The rule is meant to protect shareholders and the creditors of the company. But if the act is ultra vires (beyond the powers of) the directors only, the shareholders can ratify it. Or, if it is ultra vires the articles of association, the company can alter its articles in the proper way.

Question 7

- (a) What do you understand by ‘transmission of shares’ ? (2 marks)
- (b) Fortune Ltd. refused to enter the name of the minor son of a deceased member in the register of members on the ground that the minor cannot enter into a contract as per section 11 of the Indian Contract Act, 1872. The shares are fully paid-up. Comment on the decision of the company and suggest remedies available. (4 marks)
- (c) Piyush Ltd. decided to buy-back its shares with the approval of the Board of directors. As the Company Secretary of the company, advise the Board about the conditions and limitations in this regard. (10 marks)

Answer 7(a)

Transmission of shares – When a person dies, all his property vests at the moment of death in his legal representative. This is known as transmission or transfer by operation of law or involuntary assignment. Thus, transmission of shares takes place when the registered shareholder dies and shares in his name are transferred to his legal heir by operation of law.

Answer 7(b)

A member who is not a *sui juris* e.g., a minor, is wholly incompetent to enter into a contract and as such cannot become a member of a company. Consequently, an agreement by a minor to take shares is void *ab-initio*. Also, in India, a minor is not competent to enter into any contract as per section 11 of the Indian Contract Act, 1872.

However, in *Diwan Singh v. Minerva Films Ltd.* (1958) Comp. Cas 191, it was held that there is nothing in law to prevent minors acquiring or holding shares in a joint stock company if they are properly represented by lawful guardians. The minor is not subject to any obligation by holding paid up shares. The Company Law Board held that an agreement in writing for a minor to become a member may be signed on behalf of a minor, acting through his/her guardian, cannot be refused on the ground that the transferee is a minor, specially when the shares are fully paid up.

In the present case, the shares are fully paid up. If the minor enter into a contract on behalf of a lawful guardian, Fortune Ltd. cannot refuse to enter the name of the minor son of deceased member.

Answer 7(c)**Note from Company Secretary to the Board***Sub : Buy-back of Shares*

The Board of Directors has been considering buy-back of some shares of the company. The conditions and limitations in this regard are discussed below:

- (i) As per section 77A(1) of the Companies Act, 1956, a company can purchase its own shares, out of -
 - (a) its free reserves, or
 - (b) the securities premium account, or
 - (c) the proceeds of any shares or other specified securities.

Provided that 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.

- (ii) The buy-back of shares or securities may be in any one or more of the following modes:
 - (a) purchasing from existing security holders on a proportionate basis,
 - (b) purchasing from open market,
 - (c) purchasing from odd lot holders,
 - (d) purchasing from securities issued to employees under scheme of stock option or sweat equity.
- (iii) The following are the conditions of buy-back:
 - (a) the buy-back is authorized by its articles,

- (b) a special resolution has been passed in general meeting of the company authorizing the buy-back.
- (iv) However, the said special resolution shall not be required to be passed if the following conditions are satisfied:
 - (a) the buy-back is or for less than 10% of the total paid up equity capital and free reserves of the company, and**
 - (b) a resolution authorizing the buy-back is passed at a meeting of the Board.**

Provided that no company can come out with a fresh proposal to buy back its shares within a period of 365 days from the date of the preceding offer of buy back.

- (v) the buy-back is or less than twenty-five per cent of the total paid-up capital and free reserves of the company:

Provided that the buy-back of equity shares in any financial year shall not exceed twenty-five per cent of its total paid-up equity capital in that financial year;

- (vi) the ratio of the debt owed by the company is not more than twice the capital and its free reserves after such buy-back:

Provided that the Central Government may prescribe a higher ratio of the debt than that specified under this clause for a class or classes of companies;

- (vii) all the shares or other specified securities for buy-back are fully paid-up;
- (viii) the buy-back of the shares or other specified securities listed on any recognised stock exchange is in accordance with the regulations made by the Securities and Exchange Board of India in this behalf;
- (ix) the buy-back in respect of shares or other specified securities other than those specified in (viii) above is in accordance with the guidelines as may be prescribed.
- (x) The buy-back operations should be completed within 12 months of the date of passing of the special resolution or a resolution passed by Board.

Submitted for information and order.

Sd/-

Company Secretary

Question 8

- (a) *Can a company registered under the Companies Act, 1956 commence business of banking in India ? Discuss.* (4 marks)
- (b) *Can a listed company change its name as and when necessary ? Give reasons in support of your answer.* (4 marks)
- (c) *Grace Ltd., a public limited company has received an application from Rosy for transmission of certain shares in her name. Rosy, being a widow of a shareholder, applies for transmission of the shares standing in the name of her deceased*

husband without producing a succession certificate. Can the company transfer the shares of the deceased member ? Discuss. (4 marks)

- (d) *Vayu Ltd. holds more than 50% of nominal value of the equity capital of Stream Ltd. In these circumstances, Stream Ltd. wants to become a member of Vayu Ltd. Can Stream Ltd. do so ? Discuss the rights of the said subsidiary in such a case. (4 marks)*

Answer 8(a)

In India, banks may be set up either as a company incorporated under a Special Act of the Parliament, or as a company incorporated under the Companies Act, 1956.

As per the RBI Act, 1934, it is mandatory for a bank to get itself registered with the RBI. For registration with the RBI, a company incorporated under the Companies Act, 1956 and desirous of commencing business of banking:

- (a) should have a initial minimum paid up capital of Rs.200 crores which is to be raised to Rs.300 crores within three years of commencement of business; and
- (b) the promoters' contribution shall be a minimum of 40% of the paid up capital of the bank at any point of time.

Answer 8(b)

The name of a company can be changed by a special resolution and with the approval of the Central Government. Approval of the Central Government is not necessary if the change relates to the addition/ deletion of the word 'private' to the name. The powers of the Central Government to accord approval to the change of name, which were earlier delegated to the Regional Directors, have been delegated to the ROC w.e.f 1.7.1985 [vide Notification No. GSR 507 dated 24.6.1985].

All listed companies which decide to change their names shall be required to comply with the following conditions:

- A time period of at least one year should have elapsed from the last name change.
- At least 50% of its total revenue in the preceding one year period should have been accounted for by the new activity suggested by the new name.
- The new name along with the old name shall be disclosed through the web sites of the respective stock exchange/s where the company is listed and also through the EDIFAR web site for a continuous period of one year, from the date of the last name change. (SEB1/MRD. Policy/ AT/Cir-20/2004 dated April 30, 2004).

Answer 8(c)

Articles of companies generally provide for formalities to be observed for transmission of shares. In the absence of such provision in the articles of the company, Regulations 25 to 28 of Table A of Schedule I to the Act will govern the procedure for transmission. According to these regulations, the legal representatives are entitled to the shares held by deceased member and the company must accept the evidence of succession e.g., a succession certificate or letter of administrations or probate or any other evidence properly required by the Board of directors.

Accordingly, if a widow applies for transmission of the shares standing in the name of her deceased husband without producing a succession certificate and if the articles of association of the company so authorize, the directors of the company may dispense with the production of succession certificate, probate or letter of administration upon such terms as to indemnity as the directors may consider necessary. So, the directors may transmit the shares to the widow of the deceased by obtaining an indemnity bond.

Therefore, Grace Ltd. can transfer the shares of the deceased member to Rosy.

Answer 8(d)

A company is a holding company of another if the other is its subsidiary. For this purpose, section 4 of the Companies Act, 1956 envisages the holding of more than 50% of nominal value of the equity capital of the other company. If the holding company holds more than half in nominal value of the subsidiary's equity share capital, the relationship of holding company and subsidiary company subsists between them.

Normally, a subsidiary company cannot be a member of the holding company. However, in case where it was a member before it became a subsidiary, it shall not have the voting right at a meeting, though it may exercise other rights of members (Section 42).
