IMPORTANT QUESTIONS & ANSWERS ON COMPANY LAW - FOR – IPCC/PCC

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

ANSWER

Consequence in case of private company acting in contravention of Section 3 (1) (iii) of the Indian 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 Indian Companies Act, 1956. In accordance with the provisions of Section 43 of the Indian 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.

***2.** What is meant by a floating charge? State the characteristics of a floating charge. When does a floating charge crystallize?*

ANSWER

A floating charge is an equitable charge which is not a specific charge on any property of the company. Thus, the company may, despite the charge , deal with any of the assets in the ordinary course of business. It is of the essence of a floating charge that it remains dormant until the undertaking charged ceases to be a going concern or until the person in whose favour the charge is created, intervenes.

The main characteristics of a floating charge as described in Re. Yorkshire wool combers Association are as follows:

1. It is a charge on a class of the company's assets, present and future, that class being one which, in the ordinary course of the business is changing from time to time.
2. Generally, it is contemplated that the company carry on its business in an ordinary way with such a class of assets till some event occurs on which the charge is to settle down on the property as then existing and the charge becomes fixed. The moment the charge crystallizes, it becomes a fixed charge.

A floating charge crystallises or gets fixed when:

(i) The company goes into liquidation or

(ii) The company ceases to carry on business

(iii) A receiver is appointed or

(iv) A default is made in paying the principal and/ or interest and the holder of the charge brings an action to enforce his security.

3. *Discuss the concept of shelf prospectus, the provisions for issue and filing of such prospectus under the Companies (Amendment) Act, 2000*

ANSWER

The Companies (Amendment) Act, 2000 introduced a new section 60 A relating to the issue of Shelf Prospectus. Shelf Prospectus means a Prospectus issued by any financial institution or bank for one or more issues of securities or class of securities specified in that Prospectus.

1. Any public financial institution, public sector bank or scheduled bank whose main object is financing shall file a Shelf Prospectus. Financing means making loans to or subscribing in the capital of a private industrial enterprise engaged in infrastructural financing or such other company to be notified by the central government.

2. A company filing a Shelf Prospectus with the Registrar is not required to file Prospectus every time it seeks to make a public issue.

3. A company filing a Shelf Prospectus is required to file an Information Memorandum on all material facts relating to

(i) New charges created;

(ii) Changes in the financial position as have occurred between the first offer of securities

(iii) Previous offer of securities and the succeeding offer of securities within the time to be prescribed by the central government.

4. An Information Memorandum shall be issued to the public along with the Shelf Prospectus filed at the stage of the first offer of securities and such prospectus shall be valid for a period of one year from the date of the opening of the first issue of securities under the Prospectus. Where

an update of Information Memorandum is filed every time an offer of securities is made, such memorandum together with the shelf Prospectus shall constitute the Prospectus.

4. *What are the authorities whose approval must be sought for issue of prospectus?*

ANSWER

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 various authorities who approve the prospectus are the following:

a) All the lead managers to the issue.
b) Each of the stock exchanges where the shares of the company are listed and where the shares/debentures are proposed to be listed.
c) 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.

The Department of Company Affairs, vide its circular 10/8/87-CL V No. 7/91, dated 28-2-1991 advised the ROCs to ensure that in respect of every prospectus of public issues which comes up for filing with them the merchant bankers to the issue, whether as lead managers, co-managers, advisers or consultants are only those authorised by SEBI. Each merchant bankers has been given a code number.

It was also decided that ROC shall not register a prospectus where prior to registration of the prospectus, the ROC before whom the prospectus is filed for registration is informed by SEBI that the contents of prospectus filed are in contravention of any law or statutory rules and regulations.

In connection with the above, the SEBI has recently issued in its Circular No. 3(95-96) dated 29-9-1995, Clarification No. XII, under Guidelines for disclosure and investor protection that the draft prospectus filed with SEBI is not a public document. The final prospectus becomes available to the public only 2-3 weeks prior to the opening of the issue. To introduce greater transparency, the draft prospectus filed with SEBI would be made as a public document. The Lead managers shall simultaneously file copies of the draft document with the stock exchanges where issue is proposed to be listed, and can charge an appropriate sum to the person requesting such copy(ies).

5. *When is a director not liable for a misstatement in a prospectus?*

ANSWER

When a director is not liable [Section 62(2)] : A person who is held liable for the issue of a prospectus containing an untrue statement as a director will be exonerated from such a liability if he can show:

a) In a suit under Section 62 :
   1. that he (having consented to become a director) had withdrawn his consent to become a director before the issue of the prospectus and that it was issued without his authority or consent;
   2. that the prospectus was issued without his authority or consent; and that on becoming aware of its issue, he forthwith gave reasonable public notice of the issue having been made without his knowledge or consent; or
   3. that after the issue of the prospectus and before allotment thereunder he, on becoming aware of any untrue statement therein, had withdrawn his consent and given a reasonable public notice of the withdrawal and of the reasons therefore; or
   4. that he had reasonable ground to believe and, until allotment, did believe that the statement was true. This provision pertains to the untrue statement not purporting to have been made on the authority of an expert or of a public official document or statement.
   5. that the untrue statement, purporting to be a statement by an expert or contained in a report or valuation of an expert was a correct and fair representation of the expert's statement and he had reasonable ground to believe and, until issue of prospectus, did believe that the expert was competent to make it and the expert had given and had not withdrawn his consent to the issue of the prospectus and had not withdrawn it before delivery of a copy of the prospectus for registration; and
   6. that the untrue statement, arising from the statement made by an official person or from the public official documents was a correct and fair representation or correct copy or correct and fair extract of the document.

b) In a suit under Section 56 :

A director or other person sued for non-compliance of Section 56 may defined himself by proving :
   1. that he had no knowledge of the matter not disclosed;
   2. that the contravention was an honest mistake of fact;
   3. that in the opinion of the Court, the matter not disclosed was immaterial or was otherwise such as ought to be excused.

***6.** What is the effect of irregular allotment?*

<u>ANSWER</u>

Effect of Irregular Allotment: When the shares are not allotted in pursuance of Sections 69 and 70 such an allotment is known as irregular allotment. In spite of the stringent provisions of Sections 69 and 70, one may find that allotment has been made in utter contravention thereof. The directors may choose to take a chance and proceed to allot shares although minimum subscription has not reached or a prospectus or statement in lieu of prospectus has not been filed. Such an allotment is treated by the Act not as void ab initio but as irregular.

The applicant for the shares may avoid the allotment. If he does so within the time specified by Section 71, namely,

a) where the allotment was made before the statutory meeting, within 2 months after the holding of statutory meeting of the company and not later; or
b) where no statutory meeting is required to be held by the company, within 2 months after the date of allotment and not later; or
c) where the allotment was made after the statutory meeting within 2 months of allotment [and not later] the allotment shall be voidable despite the fact that the company is in the course of being wound up.

Within the above-mentioned period, the allottee must intimate to the company that he wants to avoid the allotment. If legal proceedings are required to be taken, these need not be within the period of two months provided the notice of avoidance was served on the company within the aforesaid time, but they should be reasonably prompt thereafter if they are required to be brought [Re. National Motor Mail Coach Co. (1908) 2 Ch. 228].

Furthermore, Sub-section (3) of Section 71 makes every director of a company, who knowingly contravenes or authorises the contravention of any of the provisions of Section 69 or Section 70 with respect to allotment, liable to compensate the company and the allottee for any loss, damages or costs which they may have sustained or incurred thereby. But the proceedings for such compensation can only be taken within two years from the date of allotment. As the allotment is only voidable at the option of the shareholder, the shareholder may keep the shares and yet sue the directors who have knowingly contravened either of the two Sections (69 and 70) to compel them to make good the loss to him as a result of the irregular allotment.

7. *Examine the different aspects of the voting rights of a member.*

ANSWER

Voting rights of a member: Section 87 governs the voting rights of members. Every holder of an equity share has the right to vote, by virtue of his share in the capital, on every resolution placed before the company. And his voting right on a poll shall be in proportion to the amount paid upon his share. A member’s right to vote may be exercised by him personally or through a proxy. Every holder of preference shares has a right to vote only on a resolution which directly affects the rights attached to the preference share capital. A resolution for the winding up of the company or repayment or reduction of its share capital is deemed to directly affect the rights of holders of preference shares. Where preference shares are cumulative as to dividend and the dividend thereon has remained unpaid for an aggregate period of not less than 2 years preceding the date of any meeting of the company, the preference shareholders shall have the right to vote on every resolution placed before the meeting.

On the other hand, if the preference shares are not cumulative as regards dividend, then the holders thereof will be able to exercise the above-mentioned extended right of voting only if dividend due on shares has remained unpaid for not less than 2 years ending with the expiry of the financial year immediately preceding the commencement of the meeting or for an aggregate period of not less than 3 years out of 6 years ending with the expiry of the financial year aforesaid. In all the above cases, the right of preference shareholders to vote on a poll shall be in the same proportion as the capital paid up on such shares bears to the total paid-up equity capital of the company. Dividend on preference shares, whether declared or not, shall be deemed to be due on the last date of the period specified for payment in the articles or other instrument executed by the company in that behalf. Alternatively, if no such date is specified, the dividend shall be deemed to be due on the day immediately following such period. The provisions stated above are, however, subject to the provisions of Sections 89 and Section 92(2) which we shall discuss here under :

A company may, be making a provision in the articles, restrain a shareholder from exercising his voting rights in respect of any shares registered in his name on which any call or other amount due has not been paid or on which the company has a lien or exercised a lien. But a public company or a private company which is a subsidiary of the public company cannot prohibit a member from voting on the ground that he has not held his share or other interest for a specified period before the time of voting or on any other ground except as mentioned above. A company may, if so authorised by its articles, accept from any member the whole or any part of the uncalled amount on shares, but the member will not be entitled to voting rights in respect of the sum paid by him until it becomes payable [Section 92]. It is in an exception to the rule that the voting rights of equity and preference shareholders on a poll will be in the same proportion as the capital paid up on those shares bears to the total paid-up equity capital.

8. *Discuss the reduction and the diminution of share capital and distinguish the two*

ANSWER

Section 100 of the Companies Act provides for the reduction of capital. For this, the articles must give the authority ; it is not enough to provide for it in the memorandum. If the articles do not so authorise, then these must be altered by a special resolution first and thereafter a second special resolution will have to be passed to reduce the capital in the manner proposed. Reduction of capital may be a reduction in the nominal capital, reduction at the same time in issued capital, a reduction in the paid-up capital or in the capital that has been issued but not paid up (e.g. where an uncalled liability is cancelled).

The term “diminution” denotes a cancellation of that portion of the issued capital which has not been subscribed for Section 94(1)(e) of the Act states it, the cancellation of “shares which at the date of the passing of the resolution in that behalf have not been taken or agreed to be taken by any person”. Section 94(3) specifically states that diminution does not constitute a reduction within the meaning of the Companies Act. The expression “diminution of share capital” and “reduction of share capital” differ from each other in the following respects.

1. Reduction may involve reduction inter alia of issued capital, whereas diminution may be in respect of authorised capital but not of issued capital.
2. If the articles authorise the procedure, diminution can be effected by an ordinary resolution, while reduction (which also need authorisation by articles), can be effected only by a special resolution.
3. Diminution needs no confirmation by the Court [Section 94(2)], but reduction needs such confirmation [Section 101].
4. Where a company is ordered to add to its name the words "and reduced" these words shall until the expiry of the period specified in the order, be deemed to be part of the company's name [Section 102(3)], but such a provision does not exist in the case of diminution of the share capital as envisaged in Section 94(1)(e).
5. In the case of diminution, notice is to be given to the Registrar within 30 days from the date of cancellation whereupon the Registrar shall record the notice and make the necessary alteration in the memorandum or articles or both [Section 95(1)(f) & (2)] ; whereas in the case of reduction more detailed procedure regarding notice to the Registrar has been prescribed by Section 103, though there is no such time limit as aforesaid (i.e. 30 days).

9. *Enumerate the particulars to be included in the Statutory Report.*

ANSWER

Statutory Report: The eight particulars to be set out in the statutory report are contained in sub-section (3) of Section 165. These are:

a) the number of shares allotted, distinguishing fully or partly paid up, otherwise than for cash and stating the extent to which the partly paid up shares have been paid and the consideration for which they have been allotted;
b) the total amount of cash received on account of shares allotted;
c) an abstract of receipts and payments up to the date within 7 days of the date of report, exhibiting under distinctive headings the receipts of the company from shares and debentures and other sources, the payment made there out and particulars concerning the balance remaining in hand and an account or estimate of the preliminary expenses of the company, showing separately any commission or discount paid or to be paid on the issue or sale of shares or debentures;
d) the names addresses and occupations of the directors and auditors, manager and secretary, if any, and any changes therein, if occurred, since the date of the company's incorporation;
e) the particulars of any contract or modifications thereof to be submitted to the meeting for its approval;
f) the extent of non-carrying of each underwriting contract together with the reason therefore;

g) the arrears due on calls from every director and manager; and
h) particulars of commission or brokerage paid or to be paid to any director for manager in connection with the issue or sale of shares or debentures.

The report aforesaid must be certified as correct by at least two directors, one of whom should be the managing director, if there be any. The auditors should also certify it to be correct insofar as the report relates to shares allotted by the company, cash received in respect thereof and receipts and payments on revenue as well as on capital account of the company.

10. *Outline some eight matters for which an ordinary resolution would suffice.*

ANSWER

Subject to the articles, an ordinary resolution is sufficient, for inter alia any of the following matters:

1. To authorise an issue of shares at a discount (Section 79);
2. To increase the share capital if authorised by the articles, or otherwise alter the share capital apart from its reduction (Section 94,100);
3. To appoint auditors [Section 224(1)]; but in the case of a company in which not less than 25 percent of the subscribed share capital is held, whether singly or in any combination, by a public financial institution or a Government company or Central or any State Government, or a nationalised bank or an insurance company carrying a general insurance business, the appointment of auditors requires a special resolution (Section 224A);
4. To appoint directors;
5. To adopt annual accounts;
6. To declare dividends;
7. To wind up voluntarily when the period, if any, fixed for the duration of the company by the articles has expired, or the event, if any , has occurred, on the occurrence of which the articles provided that the company is to be dissolved [Section 484(1)];
8. To appoint liquidators in a members 'voluntary winding-up and to fix their remuneration (Section 490);
9. To register an unlimited company as a limited company (Section 32); and generally to do all things for which a special resolution is not specifically required either by the Act or the company's articles.

11. *What are the rules relating to issue of shares at a discount?*

ANSWER

The rules relating to issues of shares at a discount is given as under : A company cannot issue shares in disregard of Section 79. It may issue at a discount, share of a class already issued, only if all the following conditions are fulfilled :

a) The issue must have been authorised by a resolution passed by the company in general meeting, and sanctioned by the Company Law Board (CLB).
b) The said resolution must specify the maximum rate of discount, at which the shares are to be issued. By virtue of the proviso added to Section 79 by the Amendment Act, 1974 no such resolution shall be sanctioned by the Company Law Board if the maximum rate of discount specified in the resolution exceeds 10 per cent unless the CLB is of the opinion that a higher percentage of discount may be allowed in the special circumstances of the case.
c) At the date of issue, not less than one year ought to have elapsed since the date on which the company was entitled to commence business.
d) Lastly, the shares to be issued at a discount have been issued within 2 months after the date of the CLB's sanction or within the time extended by it. On passing the resolution authorising the said issue, the company may apply to the CLB for its sanction thereon. Thereupon, if the CLB thinks it proper to sanction, it may do so on such terms and conditions as it thinks fit.

Every prospectus relating to issue of the shares must contain particulars of the discount allowed on the issue of the shares or so much of that discount as has been written off at the date of the issue of the prospectus. A default in compliance with this requirement will render the company, and every officer thereof who is at fault punishable with fine extending to Rs.500.

12. *Briefly examine as to what is meant by the object clause.*

ANSWER

Object clause: The powers of the company are limited to: (a) power expressly given by the memorandum (termed "express" powers) or conferred by statute, (b) powers reasonably incidental or necessary to the company's main purpose (termed "implied" powers). It may be noted that acts beyond the company's powers are ultra vires and void, and cannot be ratified even though every member of the company may give his consent [Ashbury Railway Carriage Co. vs. Riche [1875] L.R. 7 H.L. 653]. The test to be applied whether a power is implied or not, is not the benefit the transaction is expected to confer on the company, but whether it can reasonably be regarded as arising from the main object of the company.

It is customary to exclude the general rule of construction for the interpretation of the intention contained in different clauses of the memorandum of association, by including a statement that the objects specified in each paragraph of the memorandum shall be in no way limited or restricted by reference to or inference from the terms of any other paragraph or the name of the company.

The subscribers to the memorandum may choose any "object" or "objects" for the purposes of their company. There are two restrictions, however, on the selection of "object" for a company:

1. the objects should not include anything which is illegal or contrary to law or public policy, e.g., floating a company for dealing in lotteries [Ex. Parte More [1931] 2 K.B. 197]; or trading with alien enemies [Daimler & Co. vs. Continental Tyre Co. [1916] 2 A.C. 307]. Objects, which are in restraint of trade [Mac. Ellis vs. Ballymacalligot etc. Company [1919] A.C. 459] or are blasphemous (but not denying Christianity) have also been held to be bad [Bowen vs. Secular Society [1917] A.C. 406];
2. the objects should not also contemplate doing anything which is prohibited by the Companies Act. Apart from those two restrictions, the object of a company may be anything that the proposed company desires to achieve [Lal Gopal Dutt vs. Khorotriah Mego Zlite Zamindary Co. 16 C.W.N. 297].

The object clause enables shareholders, creditors and all those who deal with the company to know what its powers are and what is the range of its activities and enterprise, it is therefore true that the object clause of the memorandum of association of a company is of fundamental importance to its members as well as to its non-members.

In the first place, it gives protection to subscribers (members) who learn from it the purpose to which their money can be applied. In the second place, it protects persons dealing with the company, who can infer from it the extent of the company's powers. The narrower the objects appended in the memorandum, the lesser are the subscriber's risk; the wider these objects, the greater is the security of those who transact business with the company.

13. *"A forged transfer of shares is a nullity." Comment.*

ANSWER

A forged transfer is a nullity. It does not give the transferee concerned any title to the shares. If the company acts on a forged transfer and removes the name of the real owner from the register of Members then the company is bound to restore the name of the real owner on the register as the holder of the shares and to pay him any dividends which he ought to have received [Barton vs. North Strafford shire Railway Co. 38 Ch. D. 456. People Insurance Co. Ltd. vs. Wood & Co. Ltd. (1961) 31 Comp. Case. 63].

Thus, if by forgery, a person obtains a certificate of transfer of shares from a company and transfers the shares to a purchaser for value acting in good faith i.e. without the knowledge of the forgery, such purchaser does not get a good title to the shares so transferred, because a forged transfer is a nullity and cannot be a source of a valid transfer of title. But the company shall be liable to compensate the purchaser in so far as the company had issued a certificate to transfer and was therefore estopped from denying the liability accruing from its own act. The innocent purchaser for value acting upon the faith of the certificate issued by the company could validly and reasonably assume that the person named in the certificate as the owner of shares was really the owner of the shares represented by the certificate [Balkis Consolidated Co. vs. Tamkinson (1982) A.C. 1961]. If as a result of the forged transfer, the name of the true owner of shares is taken off the Register of Members he can compel the company to restore his name to the register.

He can also claim any dividend which may not have been paid to him during the intervening period [Barton vs. North Staffordshire Supra]. Likewise the transferee must take care that he is not getting a certificate from the company on a forged transfer, because in that case the transferee shall be liable to indemnify the company against the consequences of the damages which may have to be paid by the company to the true owner of the shares [Sheffield Corporation vs. Barclay (1905) B.C. 393]. The person who even without any negligence brings about a transfer is liable to indemnify the company against its liability to the owner of shares whose name was taken off from the register as a result of the forged transfer [Sheffield Corporation vs. Barclay (supra); Starkey vs. Bank of England (1903) A.C. 104].

14. *How can a person acquire membership of a public company? Explain in brief, whether shareholders and members are similar?*

ANSWER

Modes of Acquiring Membership: A person may become a member of the company in any one of the following ways:

1. By subscribing to the memorandum of association: The persons who subscribe (i.e. sign) to the memorandum of association are deemed to have agreed to become the members of the company. And on the registration of the company, their names are entered as members on the register of members [Section 41].
2. By application and allotment of shares: A person, who agrees in writing to become a member of the company and whose name is entered in the register of member is also a member of the company [Section 41(2)]. The person intending to become a member has to make an application to the company for the purchase of its shares. On valid allotment, the name of the shareholder is entered in the register of member.
3. By agreeing to take qualification shares: A director of a public company is appointed when he takes or signs an undertaking to take and pay for his qualification shares. When a director signs and files with the Registrar an undertaking to take and pay for his qualification shares, he is in the same position as subscriber of the memorandum of association [Section 266(2)].
4. By transfer of shares: The Companies Act provides that the shares of a public company are freely transferable. Thus, one person may transfer his shares to any other person. On the registration of transfer of shares, the transferee becomes the member of the company.
5. By succession: The legal heirs of the deceased member/shareholder get a right to be a member of the company and be registered as a member of the company on the basis of the succession certificate. The company on the basis of the Succession Certificate enters their name in the Register of Members.

A member and a shareholder: In the parlance of Company Law, the two words "member" and "shareholder", are similarly used by common people, thereby giving an impression that they are synonymous but in fact they can be differentiated on the following grounds:

a) A registered member may not be a shareholder, since a company may not be having Share Capital. For example, a company limited by guarantee and not having a share capital, does have members but not shareholders. But a registered shareholder is a member, since his name appears in the Register of Members maintained by the company.
b) A person who owns a share warrant (bearer), is not a member since his name does not appear in the Register of Members maintained by the company. He is a shareholder only [Section 115(1)].
c) A legal representative of a deceased member is a shareholder but not a member, till he applies for registration and his name is entered in the Register of members.

***15.** Illustrate, whether a limited company can become partner in a partnership firm?*

ANSWER

One of the important features of a company is an artificial juristic person. Being a juristic person, company is capable of entering contract in its own name. According to Section 4 of the Partnership Act, 1932, partnership is a contractual relationship between persons; therefore, there should not be any objection to a company in becoming partner. Further, the limited liability element of a limited company is also do not restrict a company in becoming a partner in a unlimited liability of a partnership firm, because, it is limited liability of members of a limited company and not the company itself. However, the Department of Company Affairs (now Ministry …) is in the opinion that, a company may become a partner if the Memorandum of Association specifically allows it.

***16.** Briefly explain the privileges and exemptions for a private company as provided under the Companies Act, 1956.*

ANSWER

A private company can have a greater degree of secrecy as regards its affairs and enjoys greater freedom on its operation. It enjoys some privileges and exemptions which a public company is deprived of. Briefly these are as follows:

1. Two or more persons may form a private company [Section 12(1)].
2. It need not hold a Statutory Meeting or file a statutory report [Section 165].
3. The consent of directors to act as such, and to take up qualification shares need not be filed with the Registrar [Section 266].
4. There is no restriction on the amount of overall managerial remuneration that it may pay [Section 198].
5. The directorship of a private company is not includible in the maximum number of directorships that a person may hold [Section 310].
6. The consent of the Central Government for advancing loans to directors is not required [Section 295].

7. There are no restrictions on the powers of the Board of Directors [Section 293].
8. The Central Government is not empowered to prevent a change in the Board of Directors of a company which is likely to affect management prejudicially [Section 409].
9. It can advance loans for the purchase of its own shares [Section 77(2)].

17. *What do you mean by Proxy? Explain the provisions relating appointment of Proxy under the Companies Act, 1956*

ANSWER

A proxy is an instrument in writing executed by a shareholder authorizing another person to attend a meeting and to vote thereat on his behalf and in his absence. The term is also applied to the person so appointed.

According to Section 176, the appointment of proxy must be in written instrument signed by the appointer or his duly authorized attorney. The instrument of proxy must be deposited with the company 48 hours before the meeting.

Further, unless articles otherwise provide:

1. a member of a company having no share capital cannot appoint a proxy;
2. a member of a private company cannot appoint more than one proxy to attend on the same occasion;
1. a proxy shall not be entitled to vote except on a poll.

18. *Explain the procedure for payment of Interim Dividend.*

ANSWER

A company desirous of declaring interim dividend should follow the procedure given below:

1. Verify that the Board of Directors has declared the interim dividend.
2. Ascertain whether profits for the part of the financial year up to the time of proposed declaration are sufficient to justify payment of interim dividend. Availability of profits should

be ascertained after taking into account depreciation and compulsory transfer to reserves. Auditor’s opinion should also be obtained.

3. Intimate the stock exchange(s) about the Board meeting to consider the payment of interim

dividend

4. Resolution of the Board of directors should state the rate of dividend, deposit of interim dividend in a separate account within five days from the date of its declaration, the date in reference to which shareholders registered in the Register of Members are to receive interim dividend, record date or the period of closure of the Register of Members and transfer books, date of posting of dividend warrants, etc. The Secretary may be authorized to take necessary action in this regard.

5. Inform the Stock Exchange of the date of the closure of Register of Members.
6. At least seven days before the closure of the Register of Members or the record date fixed, publish a notice in this regard in a newspaper circulating in the district in which the registered office of the company is situate.
7. Open a separate 'Interim Dividend Account' with a Bank and issue necessary instructions to the Bank.
8. Post 'Dividend Warrants' within 30 days from the declaration of interim dividend.
9. Dividend warrants to non-resident shareholders should be posted after securing necessary permission of the Reserve Bank as per the provisions of FEMA, 1999. However, if dividend balancing rule is applicable to the company paying dividend, no foreign exchange will be released.

***19.** Briefly explain the effects of Irregular allotment under the Companies Act 1956.*

ANSWER

Effect of Irregular allotment: When the shares are not allotted in pursuance of Section 69 and 70 (i.e. without receiving the minimum subscription and without filing a prospectus or statement in lieu of prospectus to the registrar before the allotment) such an allotment is an irregular allotment. In spite of the stringent provision of Section 69 and 70 one may find that allotment has been made in utter contravention thereof. The directors may choose to take a chance and proceed to allot shares although minimum subscription has not reached or a prospectus or statement in lieu of prospectus has not been filed. Such an allotment is not void initio but as irregular.
The applicant for the shares may avoid the allotment, if he does so within the time specified by Section 71, namely:

a) where the allotment was made before the statutory meeting within 2 months after the holding of statutory meeting of the company and not later; or
b) where no statutory meeting is required to be held by the company, within 2 months after the date of allotment and not later; or
c) where the allotment was made after the statutory meeting, within 2 months of allotment (and not later) the allotment shall be voidable despite the fact that the company is in the course of being wound up.

Within the aforesaid period, the allottee must intimate to the company that he wants to avoid the allotment. If legal proceedings are required to be taken, these need not be within the period of two months provided the notice of avoidance was served on the company within the aforesaid time but they should be reasonably prompt thereafter if they are required to be brought.
Furthermore, Section 71(3) makes every director of a company, who knowingly contravenes or authorizes the contravention of any of the provisions of Section 69 or Section 70 with respect to allotment, liable to compensate the company and the allottee for any loss, damages or costs which they have sustained or incurred thereby. But the proceedings for such compensation can only be taken within 2 years from the date of allotment. As the allotment is voidable at the option

of the shareholder, the shareholder may keep the shares and yet sue the directors who have knowingly contravene either of the two sections i.e. 69 and 70 to compel them to make good the loss to him as a result of the irregular allotment.

20. *Sate the types of charges to be registered with the Registrar of Companies and explain the consequences of non-registration of such charges.*

ANSWER

Types of Charges to be registered and Consequences of Non-Registration: Section 125 and 127 of the Companies Act, 1956 require the companies to get registered the following charges with the Registrar of Companies within 30 days of their creation:

1. a charge for the purpose of securing any issue of debentures.
2. a charge on uncalled share capital of the company
3. a charge on any immovable property, wherever situate or any interest therein.
4. a charge on any book debt of the company.
5. a charge not being a pledge, on any movable property of the company.
6. a floating charge on the undertaking or any propertuy of the company including stock in trade.
7. a charge on calls made but not paid.
8. a charge on a ship or any share in a ship.
9. a charge on goodwill, on a patent or licence under a patent, on a trade mark or on a copy right or a licnece under a copy right.
10. a charge created out of India comprising solely property situate outside India with particulars and the instrument creating or evidencing the charge or a copy thereof.
11. a charge created in India comprising property outside India will the instrument creating or purporting to create the charge or a verified copy thereof (Section 125).
12. a charge on a property acquired subject to charge (Section 127).

21. *What is red-herring prospectus? Briefly explain the information memorandum.*

ANSWER

"Red-herring prospectus" means a prospectus which does into have complete particular on the price of the securities offered and the quantum of securities offered.

1. A public company making an issue of securities may circulate information memorandum to the public prior to filing of a prospectus.
2. 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 a red-herring prospectus, at least three days before the opening of the offer.
3. The information memorandum and re-herring prospectus shall carry same obligations as are applicable in the case of a prospectus.

4. Any variation between the information memorandum and the red-herring prospectus shall be highlighted as variations by the issuing company.
5. Every variation as made and highlighted in accordance with Sub-section (4) above shall be individually intimated to the persons invited to subscribe to the issue of securities.
6. The applicant or proposed subscriber shall exercise his right to withdraw from the application on any intimation of variation within seven days from the date of such intimation and shall indicate such withdrawal in writing to the company and the underwriters.

22. *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.*

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 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 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.

23. *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.*

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.

<u>The following steps are required to be taken for such conversion:</u>

a) Board must fix the date for general meeting for the purpose of making necessary alternation in the Articles of Association and Memorandum of Association.

b) 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(i) (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 on the date of alteration company. 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.
c) 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
d) 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.
e) The company must ensure the minimum number of members is 7, of directors is 3 and the paid up capital is not less than Rs. 5 lakhs.

24. *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 tow member companies.

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 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 represents two members 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.

25. *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.*

ANSWER

Buy-back of shares sources and conditions (Sec. 77 A of the Companies Act, 1956): In accordance with the provisions of the Companies Act, 1956, as contained in sec. 77-A, 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 A/c; or
3. Out of the proceeds of any shared or other specified securities. {S.77-A-(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 authorizing 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.

26. *XYZ Limited called its Annual General meeting on 28th September, 2007. The notice of the meeting was posted on 6th September, 2007. With reference to the provisions of the Companies Act, 1956 examine whether the notice given by the company was valid.*

ANSWER

Length of notice for Annual General Meeting

According to section 171 (1) of Companies Act 1956, a general meeting of a company may be called by giving not less than 21 days notice in writing not less than 21 days means 21 clear days i.e. excluding both the dates on which the notice was served and the date of the meeting. In case the notice of the meeting was sent by past, service of the notice of the meeting shall be deemed to have been effected at the expiry of 48 hours after it was posted {Section 53 (2) (b) (i)). In the instant case, the notice was short by one day as shown below:

6th September 2007 to 28th September 2007	23 days
Less date of service and date of meeting	2 days
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	21 days
Less 48 hours of posting but 24 hours are common between date of service and 48 hours of posting	1 day
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	20 days
Length of notice required	21 days

Short notice	1day

Hence the notice was not valid.

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 Indian Companies Act, 1956 ?*

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.

28.*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.*

ANSWER

According to Section 36(1) of the Indian 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).

29. *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 Indian Companies Act, 1956.*

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.

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

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 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.