

Board's Powers and Restrictions Thereon (Sections 291 – 293)

General Powers of the Board (Section 291)

Question 1

M/s ABC Ltd. had power under its memorandum to sell its undertaking to another company having similar objects. The Articles of the company contained a provision by which directors were empowered to sell or otherwise deal with the property of the company. The Shareholders passed an ordinary resolution for the sale of its assets on certain terms and required the directors to carry out the sale. The Directors refused to comply with the wishes of the shareholders where upon it was contended on behalf of the shareholders that they were the principal and directors being their agents were bound to give effect to their decision. Based on the above facts, decide the following issues, having regard to the provisions of the Companies Act, 1956 and case laws.

- (i) *Whether the contention of shareholders against the non-compliance of their wishes by the directors is tenable.*
- (ii) *Can shareholders usurp the powers which by the articles are vested in the directors by passing a resolution in the general meeting?* **(November 2007)**

Answer

General Powers vested in the Board of Directors:

The provisions relating to the general powers which are vested are given under Section 291 of the Companies Act, 1956. As per this section, the Board of Directors of a company is entitled to exercise all such powers and to do all such acts and things as the company is authorized to exercise and do. This means the powers of the Board of Directors are co-extensive with those of the company. The proposition is, however subject to two conditions:

Firstly, the Board shall not do any act which is to be done by the company in general meeting. Secondly, the Board shall exercise all such powers subject to the provisions contained in the Companies Act, 1956 or in the Memorandum or the Articles of the Company or in any regulations made by the Company in general meeting. But no regulation made by the company in general meeting shall invalidate any prior act of the Board which would have been valid if that regulation had not been made.

It is the first and elementary principle of company law that when powers are vested in the Board of directors by the Articles of a company, they cannot be interfered with by the shareholders as such (*Murarka etc. Works Ltd. vs. Mohal Lal AIR (1961) Col 251*).

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In exercising their powers the directors do not act as agent for the majority members or even all the members. The members therefore cannot by resolution passed by a majority or even unanimously supersede the powers of directors or instruct them how they shall exercise their powers. The above problem is based on decision given by the *Chancery Court in the case Automatic Self Cleansing Filter Syndicate Co. Ltd. Vs. Cunninghame (1906) 2ch 34* and this case also followed in India in *MPLV Works vs Murarka AIR 1961 Col 251*.

In view of above discussion, the contention of shareholders against the non-compliance of their wish by the directors is not tenable and shareholder cannot usurp the power which by articles vested in the directors by passing even a resolution of a numerical majority at the general meeting. The shareholders have, however, the power to alter the Articles of Association of the company in the manner they like subject to the provisions of the Companies Act, 1956.

Certain powers to be exercised by Board only at meeting (Section 292)

Question 2

Out of the powers exercisable by the Board under section 292, the board wants to delegate to the Managing Director of the company the power to borrow monies otherwise than on debentures. Advise whether such a delegation is possible? Would your answer be different, if the delegation is given to the manager or any other principal officer including a branch officer of the company?

Answer

According to Section 292, the following powers can be exercised by the Board only by means of resolution passed at its meetings:

- (a) to make calls; (aa) to authorise the buy back of shares
- (b) to issue debentures;
- (c) to borrow money otherwise than on debentures;
- (d) to invest the funds of the company;
- (e) to make loans.

The Board may, however, by resolution passed at meeting, delegate the last three powers mentioned above to the extent specified hereunder. Such a delegation can be made to any committee of directors, the managing director, the manager or any other principal officer of the company or in the case of a branch office of the company, a principal officer thereof. Every resolution delegating the power referred to in (c), (d) and (e) above shall specify: (i) the total amount outstanding at any time up to which money may be borrowed by the delegate; (ii) the total amount up to which the funds may be invested as well as the nature of investment; and (iii) the total amount of loans and the purpose thereof up to which and for which loans may be raised respectively. It is to these extents that the delegate may exercise the aforesaid three

powers. The company in general meeting may impose restrictions and conditions on the exercise by the Board of any of the five powers mentioned above.

In connection with the power mentioned in (c) above, a question may arise whether borrowing on a promissory note is within the powers of the directors.

It has been held in [*P. Rangaswami Reddiar and Another vs. R. Krishnaswami Reddiar and another* (1971) 43 Comp. Case 232] that where such a borrowing permissible under the company's articles and moneys were borrowed on promissory notes, such transaction would come within the powers of the director. It has also been held in the same case that where a person was appointed as the managing director of the company by the Board's resolution vested with full powers of the management of the affairs of the company and authorised to sign all the papers of the company, he would have full powers to borrow money on a promissory note even without a resolution of the Board as contemplated by Section 292(c) of the Act.

Question 3

The Directors of X & Co. Ltd. desire to authorise the Managing Director to enter into the following transactions namely-

- (a) *invest from time to time surplus funds in the purchase of shares of other companies:*
- (b) *borrow from banks money required for the purpose:*
- (c) *give loans to persons, including firms in which directors or their relatives are partners and*
- (d) *give donations to charitable trusts in which any of the directors may be interested as trustees.*

State whether these delegated powers are within the purview of the relevant provisions of the Companies Act, 1956.

Answer

- (a) Although Section 292 empowers the Board of Directors of a company to delegate to the Managing Directors the power to invest, in general terms, the funds of the company nevertheless because of the overriding provisions of Section 372(5) (which Section we shall discuss in detail in Study paper 3), the transaction in the instant case would be invalid. Section 372(5) provides that no investment in shares of a company can be made by the Board of Directors of an investing company in pursuance of sub-section (2), unless it is sanctioned by a resolution passed at a meeting of the Board with the consent of all the directors present at the meeting except those not entitled to vote thereat, and unless further notice of the resolution to be moved at the meeting has been given to every director in the manner specified in Section 286. Since Section 372 does not provide for delegation of the power, the proposed delegation to the Managing Director in question, notwithstanding the general provision of Section 292, cannot be made.

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- (b) In terms of Section 292 the Board of Directors may also delegate to the Managing Director the power to borrow money otherwise than debentures, which it can exercise only by means of resolutions passed at Board meetings. As per Explanation to Section 292(1), it is the arrangement for an overdraft or cash credit that constitutes the exercise of the borrowing power and not the actual utilisation of the arrangement. In other words, an arrangement for an overdraft or cash credit to the tune of say Rs.5 lakhs constitutes the exercise of the borrowing power and not the actual drawing of this amount on the basis of the overdraft or cash credit. Consequently, the transaction in the instant case shall be valid. But before implementation of the proposal, the Board must pass a resolution at its meeting authorising the Managing Directors to borrow from banks money required for the purpose of the company's business. Also the resolution delegating this power shall specify the total amount outstanding at any one time up to which the delegate may borrow money.

If however, the moneys to be borrowed together with the money already borrowed by the company (apart from temporary loans obtained from the Company's bankers in the ordinary course of business) will exceed the aggregate of the paid up capital of the company and its free reserves, [that is to say, reserves not set apart for any specific purpose] the Board of Directors of the company in question must obtain the consent of the company in its general meeting. Consequently, care should be taken to ensure that while delegating the power to the managing director the aforesaid provision has not been violated; also it should be ensured that the memorandum of association permits borrowing.

- (c) Since according to Section 295(1), (which we shall discuss later) without obtaining prior approval of the Central Government in that behalf, a company can not directly or indirectly lend money to persons including firms, in which directors or their relatives are partners, the company in question must in the first instance seek the Central Government's approval. Secondly since the power to make loans may be delegated under Section 292(1)(e), the Board of Directors of the company in question must pass a resolution therefore and every resolution delegating this power to the Managing Director shall specify the total amount up to which loans may be made by the delegate, the purpose for which loans may be made and the maximum amount of loans which may be made for each such purpose in individual cases. Thirdly, by virtue of Section 291(1), the Board must see with reference to the memorandum and articles whether the company is authorised to exercise the power.
- (d) Under Section 293(1) (e), the Board of Directors of a public company can contribute or donate to charitable and other funds not directly related to the business of the company or the welfare of its employees any amount the aggregate of which will not, in any financial year exceed Rs.50,000 or 5% of its average net profits during the three financial years preceding whichever is greater. If this power of the company is not *ultra vires* the memorandum of the company, then only the Board can act in pursuance of the above-mentioned resolution of the company and in so acting, it can authorise the Managing Director to exercise the power on behalf of the Board.

It may be noted that the power of the Board to donate to general charities is not conditional to the existence of any profits. In such case, they may contribute up to the limit given in Section 293(1)(e), even though the company may be working at a loss.

Question 4

A Managing Director was authorized by the Board to borrow money on a Promissory Note. State in this connection whether borrowing on a promissory note is within the powers of the directors.

Answer

It has been held in [*P. Rangaswami Reddiar and Another vs. R. Krishnaswami Reddiar and another* (1971) 43 Comp. Case 232] that where such a borrowing permissible under the company's articles and moneys were borrowed on promissory notes, such transaction would come within the powers of the director. It has also been held in the same case that where a person was appointed as the managing director of the company by the Board's resolution vested with full powers of the management of the affairs of the company and authorised to sign all the papers of the company, he would have full powers to borrow money on a promissory note even without a resolution of the Board as contemplated by Section 292(c) of the Act.

Question 5

M/s Hurybury Builders Limited is contemplating to enter into a joint venture agreement with another construction company for the development of landed properties located at Bangalore. Since it is not possible to convene the Board Meeting immediately, as the directors are at different places in connection with various works, the Managing Director seeks your advice on the following matters:

- (i) *Whether the resolution pertaining to the joint venture agreement is required to be passed at the Board Meeting convened for this purpose or whether it can be passed by means of a circular resolution.*
- (ii) *What are the resolutions that are required to be passed only at the meetings of the Board of Directors?*
- (iii) *The steps that are required to be taken to pass the Board resolution by circulation. Advise.*

(May, 2002)

Answer

The directors of the company act together as a body and generally at the meeting of the Board duly convened, unless special powers are delegated to an individual director or the managing director. Where it is not possible to hold board meetings because the directors are busy elsewhere or the time for convening such a meeting is short, it is possible that the required resolution can be passed by way of circular resolution as provided in section 289 of the Companies Act, 1956. However, under section 292, certain powers can be exercised by the Board of directors only by means of a resolution passed at meeting convened for this purpose.

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They are (i) to make calls (ii) to issue debentures (iii) to borrow money otherwise than on debentures (iv) to invest the funds of the company and (v) to make loans. In view of the above, the Managing Director can go ahead and complete the joint venture agreement after obtaining the approval of the board by passing a circular resolution. For this purpose, the proposed resolution has to be circulated in draft along with the other necessary papers, if any, to all the directors in India at their usual residential addresses. The resolution will become valid if the same is approved by majority of the directors and who are entitled to vote on the resolution. There after the resolution as passed by way of circulation will be entered in the minutes book of the Board of Directors and is enough compliance of the provisions of Companies Act in this regard.

Question 6

Advise the Board of Directors of a public company about their powers in respect of the following proposals explaining the relevant provisions of the Companies Act, 1956:

- (i) *Donation of ₹ 5,00,000 to a hospital established exclusively for the benefit of employees.*
- (ii) *Buy-back of shares of the company for the first time upto 10% of the paid-up equity share capital.*
- (iii) *Delegating to the managing director of the company the power to invest surplus funds of the company in the shares of some companies.* **(May, 2003)**

Answer

- (i) **Donation to a hospital run exclusively for the benefit of employees of the company:** The limit of 5% of average net profits during the last 3 financial years is applicable only to contributions to charitable and other funds not directly relating to the business of the company or the welfare of its employees [Section 293(1)(e), Companies Act, 1956]. Hence the Board is empowered to make the proposed donation to the hospital.
- (ii) Section 292 has been amended by Companies (Amendment) Act 2001 to facilitate buy back of shares upto 10% of the total paid-up equity capital and free reserves [Section 292(i)(aa)]. Hence special resolution in general meeting of the company is not required. Hence the proposed buy back of shares is in order provided other conditions laid down on section 77A are fulfilled.
- (iii) Section 292 of the Companies Act, 1956, empowers the Board of Directors to delegate to the M.D the power to invest in general terms. But Section 372A(2) provides that no investment shall be made, unless it is sanctioned by a resolution passed at a meeting of the Board with the consent of all the directors present Section 372A does not provide for delegation. Hence the proposed delegation of power to invest to the M.D. is not in order.

Question 7

Decide in the light of the provisions of the companies Act, 1956 the validity and extent of powers of Board of Directors and the procedure to be complied with in the following matters:

- (i) *Delegation of power of the Managing Director of the company to invest surplus funds of the company in the shares of some companies.*
- (ii) *Donation of Rs.5 lakhs to a hospital established exclusively for the benefit of employees and a donation of Rs.5 lakhs to a charitable trust registered under Section 12A and exempted under Section 80G of the Income-tax Act, 1961.*
- (iii) *Donation of Rs.5 Lakhs to a political party registered with the appropriate authority.*

(June 2009)

Answer

- (i) Section 292 of the Companies Act, 1956 empowers the Board of Directors to delegate to the Managing Director the power to invest in general terms. But section 372A (2) of the said act provides that no investment shall be made, unless it is sanctioned by a resolution passed at a meeting of the Board with the consent of all the directors present. Section 372A does not provide for delegation. Hence the proposed delegation of power to the Managing Director to invest is not in order.

- (ii) Donation to a hospital run exclusively for the benefit of employees of the company is in order. The limit of 5% of average net profits during the last three financial years is applicable only to contributions to charitable and other funds not directly relating to the business of the company or the welfare of its employees. Thus, under section 293 (1) (e) of the Companies Act, 1956, the Board is empowered to make the proposed donation to the hospital.

However the donation of Rs.5 Lakhs to a charitable trust is subject to the limit laid down in section 293(1) i.e. Rs.50,000 or 5% of the average net profits of the company during the last three financial years whichever is higher.

Thus to contribute Rs.5 lakhs the average net profits for last three financial years should be Rs.100 lakhs.

- (iii) Donation of Rs.5 Lakhs to a political party can be made if the company is in existence for more than 3 years and the donation amount cannot exceed 5% of the average net profit for the preceeding three years. Further the procedure laid down in Section 293 A should also be complied with.

Question 8

Advise the Board of Director of Spectra Papers Ltd. regarding validity and extent of their powers, under the provisions of the Companies Act, 1956 in relation to the following matters:

- (i) *Buy-back of the shares of the Company, for the first time, upto 10% of the paid up equity share capital without passing a special resolution.*

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- (ii) *Delegation of Power to the Managing Director of the company to invest surplus funds of the company in the shares of some companies. (CA Final, New Course, May, 2010)*

Answer

- (i) Section 292 (i) (aa) of the Companies Act, 1956 facilitates buy-back of shares upto 10 % of the total paid up equity capital and free reserves. Hence, special resolution in general meeting of the company is not required. The proposed buy-back of shares is in order provided other conditions laid down in Section 77A of the Companies Act, 1956 are fulfilled.
- (ii) Section 292 of the Companies Act, 1956 empowers the Board of Directors to delegate to the Managing Director the power to invest in general terms. But Section 372A (2) of the said Act provides that no investment shall be made unless it is sanctioned by a resolution passed at a meeting of the board with the consent of all Directors present. Section 372A does not provide for delegation. Hence the proposed delegation of power to the Managing Director to invest is not in order

Question 9

A is the Director of M & Co. Ltd. A has borrowed ` 50/- lacs on reasonable terms from X for company's benefit and business. A has no power to borrow. What will be the legal position? Please explain.

(CA Final, New Course, November, 2010)

Answer

Money has been borrowed and used for the benefit of the company and its legitimate business purposes. Therefore, the company cannot repudiate the liability on the ground that the director 'A' has no power to borrow. (*LTR. Practice (Bombay) vs E.D.SASSR & Co. (1936) 6 Comp Cases 90*).

In light of the above, company itself would be liable to pay. 'A' a director stands in a fiduciary relationship with the company (*City Equitable Insurance Co (1925) Ch 407*)

Audit Committee (Section 292A)

Question 10

An Audit Committee of a Public Limited Company constituted under section 292A of the Companies Act, 1956 submitted its report of its recommendation to the Board. The Board, however, did not accept the recommendations. In the light of the situation, analyze whether:

- (a) *The Board is empowered not to accept the recommendations of the Audit Committee.*
- (b) *If so, what alternative course of action, would be Board resort to?*
- (c) *As a Chairman of the Audit Committee, how would you respond to the situation?*

Answer

- (i) As per Section 292A, a recommendations of the audit Committee on any matter relating to financial management, including the audit report, shall be binding on the Board.

- (ii) If the Board does not accept the recommendations of the Audit Committee, it shall record the reasons therefore and communicate such reasons to the shareholders.
- (iii) The Chairman of the Audit Committee shall attend the Annual General Meeting(s) of the company to provide any clarifications on matters relating to Audit.

Question 11

The paid-up capital of XYZ Limited has been increased from Rs.4 crores to Rs.6 crores. The Board of Directors of XYZ Limited purpose to constitute an 'Audit Committee'. At present the board consists of 10 directors including a Managing Director. Draft a board resolution taking into account the requirements under the Companies Act relating to the constitution of the Audit Committee and the chairman of the audit Committee. XYZ Limited is not a listed public company.
(May, 2002)

Answer

- (1) As per section 292A of Companies Act, 1956, every public company having paid up capital of ₹ 5 cores or more must constitute a committee of Board as 'Audit Committee'.
- (2) The audit committee shall consist of minimum 3 directors. Out of the total members of committee, at least two-third shall be on executive directors, that is those who are not managing or whole time directors. The committee shall elect its own Chairman. Terms of reference will be specified in writing by the Board (Section 292A(2)).
- (3) *Draft Board resolution.*

"Resolved that, pursuant to section 292A of the Companies Act, 1956 an Audit committee consisting of the following directors be and is hereby constituted

- 1. Shri_____, Nominee of IFCI
- 2. Shri_____, Nominee of IDBI
- 3. Shri_____,
- 4. Shri_____,
- 5. Shri_____, Managing Director

Further resolved that the Chairman of the Audit Committee shall be elected by its members from amongst themselves. Further resolved that the Audit Committee shall have the authority to investigate into any matter what may be prescribed under the said section 292 A and the following matters

- 1. _____
- 2. _____
- 3. _____
- 4. _____ "

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Question 12

MNC Ltd., a company, whose paid up capital was ₹ 4.00 Crores, has issued rights shares in the ratio of 1:1. The said company is listed with Mumbai Stock Exchange. Whether the company is required to appoint any Audit Committee and if yes, draft a suitable Board Resolution to appoint an Audit committee covering the aspects as provided in the Companies Act, 1956 and the listing Agreement with the Stock Exchange. In case the company is not required to appoint any Audit Committee, state the provisions of the Companies Act, 1956 in respect of appointment of Audit Committee by a Company. (May 2007)

Answer

As per provision of section 292A of the Companies Act, 1956, a public company having a paid up capital of ₹ 5.00 Crores or more is are required to have an Audit Committee. Since, after the rights issue by MNC Ltd. its paid up capital has increased to ₹ 8.00 Crores, it is required to appoint an Audit Committee.

The relevant Board Resolution for appointment of an Audit Committee is as follows:

“Resolved that pursuant to the provision contained in section 292A of the companies Act 1956 and clause 49 of Listing Agreement with the Mumbai Stock Exchange, an Audit Committee of the Company be and is hereby constituted as under:

1. Mr. A -- An Independent Director.
2. Mr. B -- An Independent Director
3. Mr. C -- Director nominated by IDBI
4. Mr. D -- An Independent Director
5. Mr. FD -- Financial Executive
6. Mr. MD -- Managing Director

Further resolved that the Chairman of the Committee, who shall be an independent Director, be elected by the members from amongst themselves.

Further resolved that the quorum for a meeting of the Audit Committee shall be 1/3rd of the total number of members or two directors (other than the Managing Director), whichever is higher.

Further resolved that the Audit Committee shall comply with the following:

- (1) The Audit Committee shall have meetings periodically as it may deem fit with at least three meeting in a year, viz., one meeting before finalization of annual accounts and one every six months.
- (2) The Audit Committee shall invite such of the executives (and particularly the head of the finance function) to be present at the meeting of the Committee whenever required by it.
- (3) The finance Director, head of internal audit and the auditors of the company shall attend and participate at the meeting without right to vote.

Further resolved that the audit Committee shall have the authority to investigate into any matter that may be prescribed under the said section 292A of the Companies Act, 1956 and the matters as mentioned in the Listing Agreements entered into between the Company and the Mumbai Stock Exchange and all the matters as may be referred to it by the Board from time to time and for this purpose the Audit Committee shall have full access to information contained in the records of the Company and external professional advice, if necessary.

Further resolved that the Audit committee shall conduct discussions with the auditors periodically about internal control system, the scope of audit including the observations of the auditors.

Further resolved that the Audit Committee shall review the quarterly and annual financial statements and submit the same to the Board with its recommendations, if any.

Further resolved that the recommendations made by the Audit Committee on any matter relating to financial management including the audit report shall be binding on the Board. However, where such recommendations are not accepted by the Board, the reasons for the same shall be recorded in the minutes of the Board meeting or communicated to the shareholders.

Further resolved that the Audit Committee have the minutes of its meetings drawn and approved by the Chairman of the Committee and the same be circulated to the members of the Board within thirty days from the date of such meeting.

Further resolved that the Company Secretary of the Company shall be the Secretary to the Audit Committee.

Further resolved that the Chairman of the Audit Committee shall attend the annual general meeting of the Company to provide any clarifications on matters relating to audit as may be required by the members of the company.

Further resolved that the Board's Report/Annual Report to the members of the Company shall include the particulars of the constitution of the Audit Committee."

Question 13

Supra Limited, a private company, has been converted into a public company and under the provision of the Companies Act, 1956. The company proposes to constitute an audit committee. Taking into account the provisions of the Companies Act, 1956 draft a board resolution covering the following matters:

- (i) *Member of the audit committee.*
- (ii) *Chairman of the audit committee.*
- (iii) *Quorum for meeting of the said committee.*
- (iv) *Any two functions of the said committee.*

(May 2003)(November 2008)

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Answer

AUDIT COMMITTEE – BOARD’S RESOLUTION:

“Resolved that pursuant to Section 292A of the Companies Act, 1956 an Audit Committee consisting of the following Directors be and is hereby constituted.

1. Mr. ---- Nominee of IDBI
2. Mr. ---- Nominee of ICICI
3. Mr. ---- Nominee of the SBI.
4. Mr. ---
5. Mr. ----- Managing Director.

Further resolved that the Chairman of the Audit Committee shall be elected by its members from amongst themselves.

Further resolved that the quorum for a meeting of the Audit committee shall be 1/3rd of the total number of members or two directors (other than the Managing Director) whichever is higher.

Further resolved that the Audit Committee shall have the authority to investigate into any matter that may be prescribed under Section 292A of the Companies Act, 1956 and any other matter that may be referred to it by the Board from time to time.

Further resolved that the Audit committee shall conduct discussion with the auditors periodically about internal control systems, the scope of audit including the observation of auditors.

Further resolved that the Audit Committee shall review the quarterly and annual financial statements and submit the same to the Board with its recommendations if any”.

Question 14

Explain how the provisions of the Companies Act, 1956 relating to Audit Committee will help in achieving some of the objectives of Corporate Governance.

(May 2005) (CA Final, New Course, May 2009)

Answer

For better corporate governance the concept of Audit committee for companies was introduced by section 292A of the Companies Act, 1956. Every public company having paid up capital of not less than Rs.5.00 crores must have an audit Committee.

The auditors, the internal auditor, if any and the Director-In-Charge of finance shall attend and participate at meetings of the Audit Committee [Section 292A (5)]

As per Section 292A(6) of the said Act, the functions of the Audit Committee includes the following:

- (a) The Audit Committee should discuss with the auditors periodically about internal control systems, the scope of audit including the observations of the auditors.

- (b) The Audit Committee should review half yearly and annual financial statements before submission to the Board.
- (c) The Audit Committee should ensure compliance of internal control systems.

The Audit committee shall have authority to investigate into any matter in relation to the items specified in this Section or referred to it by the Board and for this purpose, shall have full access to information contained in the records of the company and external professional advice, if necessary. [Section 292A (7)].

The recommendations of the Audit Committee on any matter relating to financial management including the audit report shall be binding on the Board and if the Board does not accept the recommendations of the Audit Committee, it shall record the reasons therefore and communicate such reasons to the shareholders. (Section 292A (8) & (9)).

The above provisions of law relating to powers and functions of the Audit committee relating to financial statements will help in achieving one of the objective of corporate governance i.e. accountability and avoidance of poor financial reporting.

Restrictions on powers of Board (Section 293)

Question 15

The Board of Directors of Stepping Stones Publications Ltd. at a meeting held on 15.1.2001 resolved to borrow a sum of ₹ 15 crores from a nationalized bank. Subsequently the said amount was received by the company. One of the Directors, who opposed the said borrowing as not in the interest of the company has raised an issue that the said borrowing is outside the powers of the Board of Directors. The Company seeks your advice and the following data is given for your information:

- (i) Share Capital ₹ 5 crores
- (ii) Reserves and Surplus ₹ 5 crores
- (iii) Secured Loans ₹ 15 crores
- (iv) Unsecured Loans ₹ 5 crores

Advise the management of the company.

(May, 2001)

Answer

According to the provisions of Section 293(1)(d) of the Companies Act, 1956 there are restrictions on the borrowing powers to be exercised by the Board of directors. According to that section, the borrowings should not exceed the aggregate of the paid up capital and free reserves. While calculating the limit, the temporary loans obtained by the company from its bankers in the ordinary course of business will be excluded. However, from the figures available in the present case the proposed borrowing of ₹ 15 crores will exceed the limit mentioned. Thus the borrowing will be beyond the powers of the Board of directors. However the share holders have the power to ratify the act of the Board of Directors, if it is not beyond the powers of the company as laid down in the memorandum of association. In that case the

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shareholders can ratify as it is intra vires the company even though it may be beyond the powers of the Board of Directors.

Thus the management of Stepping Stone Publications Ltd., should take steps to convene the annual general meeting and pass a resolution by the members in the meeting as stated in Section 293(1)(d) of the Act. Then the borrowing will be valid and binding on the company and its members.

Question 16

The Balance Sheet of International Operators Ltd as at 31-03-2011 disclose the following position

	₹ (in crores)
Share Capital	100
Reserves & Surplus	300
Secured Loans	150
Unsecured Loans	100
Current Liabilities	70

Mr X, the Managing Director of the company approaches the Royal Bank for a secured loan of ₹ 600 crores to finance the new projects to be taken up shortly. The Bank seeks your advise whether it can grant the loan of ` 600 crores on the application of Mr. X. Advise the Royal Bank having regard to the provisions of the Companies Act, 1956. **(May 2011)**

Answer

Powers of directors related to borrowing funds by the company:

The management of Royal Bank should be aware of the provisions of Sections 292 and 293 of the Companies Act, 1956, which govern the powers of directors in the matter of borrowing funds by the company. According to Section 292, the Board of Directors of International operators Ltd. can exercise the borrowings by passing a resolution at a duly convened meeting of the Board of Directors. However, under Section 293, the Board of Directors of a public company cannot, except with the consent of the members of the company in general meeting borrow moneys, where the moneys to be borrowed together with the moneys already borrowed by the company, exceeds the aggregate of the paid up capital of the company and its free reserves.

In the present case, the proposal of the company to borrow ₹ 600 crores exceed the paid up share capital and free reserves of the company to the tune of ₹ 200 crores (i.e. ₹ 600 crores – ₹ 400 crores = ₹ 200 crores) without taking into account the existing loan. Thus Royal Bank should advise Mr. X, the Managing Director of the company to get the approval of the shareholders of the company as provided in Section 293 before considering the request of the company for a loan of ₹ 600 crores. In case, the loan is secured by mortgaging the assets of the company the bank should also ensure that the particulars of the charge are registered with the Registrar of Companies as provided in Section 125 of the Companies Act, 1956.

Question 17

The last three years' Balance Sheet of PTL Ltd., contains the following information and figures:

	As at 31.03.2003 ₹	As at 31.03.2004 ₹.	As at 31.03.2005 ₹.
Paid up capital	50,00,000	50,00,000	75,00,000
General Reserve	40,00,000	42,50,000	50,00,000
Credit Balance in Profit & Loss Account	5,00,000	7,50,000	10,00,000
Debenture Redemption Reserve	15,00,000	20,00,000	25,00,000
Secured Loans	10,00,000	15,00,000	30,00,000

On going through other records of the Company, the following is also determined:

Net Profit for the year (as calculated in accordance with the provisions of Section 349 & 350 of the Companies Act, 1956)	12,50,000	19,00,000	34,50,000
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In the ensuing Board Meeting scheduled to be held on 5th November, 2005, among other items of agenda, following items are also appearing:

- (i) *To decide about borrowing from Financial institutions on long-term basis.*
- (ii) *To decide about contributions to be made to Charitable funds.*

Based on above information, you are required to find out as per the provisions of the Companies Act, 1956, the amount upto which the Board can borrow from Financial institution and the amount upto which the Board of Directors can contribute to Charitable funds during the financial year 2005-06 without seeking the approval in general meeting.

(November 2004, November 2005)

Answer

- (i) **Borrowing from Financial Institutions:** As per Section 293(1)(d) of the Companies Act, 1956, the Board of Directors of a public company or a private company which is a subsidiary of a public company, without obtaining the approval of shareholders in a general meeting, can borrow the funds including funds already borrowed upto an amount which does not exceed the aggregate of paid up capital of the company and its free reserves. Such borrowing shall not include temporary loans obtained from the company's bankers in ordinary course of business. Here, free reserves do not include the reserves set apart for specific purpose.

Since the decision to borrow is to be taken in a meeting to be held on 5th November, 2005, the figures relevant for this purpose are the figures as per the Balance Sheet as

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at 31.03.2005. According to the above provisions, the Board of Directors of PTL Ltd. can borrow, without obtaining approval of the shareholders in a general meeting, upto an amount calculated as follows:

	₹
Paid up Capital	7,500,000
General Reserve (being free reserve)	5,000,000
Credit Balance in Profit & Loss Account (to be treated as free reserve)	1,000,000
Debenture Redemption Reserve (This reserve is not to be considered since it is kept apart for specific purpose of debenture redemption)	----
Aggregate of paid up capital and free reserve	13,500,000
Total borrowing power of the Board of Directors of the company, i.e, 100% of the aggregate of paid up capital and free reserves	13,500,000
Less: Amount already borrowed as secured loans	3,000,000
Amount upto which the Board of Directors can further borrow without the approval of shareholders in a general meeting.	10,500,000

- (ii) **Contribution to Charitable Funds:** As per Section 293(1)(e) of the Companies Act, 1956, the Board of Directors of a public company or a private company which is a subsidiary of a public company, without obtaining the approval of shareholders in a general meeting, can make contributions to charitable and other funds not directly related to the business of the company or the welfare of its employees upto an amount which, in a financial year, does not exceed Rs.50,000/- or five per cent of its average net profits as determined in accordance with the provisions of Sections 349 and 350 of the Companies Act, 1956 during the three financial years immediately preceding, whichever is greater.

According to the above provisions, the Board of Directors of the PTL Ltd. can make contributions to charitable funds, without obtaining approval of the shareholders in a general meeting, upto an amount calculated as follows:

Net Profit for the year (as calculated in accordance with the provisions of Sections 349 & 350 of the Companies Act, 1956:

	₹
For the financial year ended 31.12.2003	12,50,000
For the financial year ended 31.12.2004	19,00,000
For the financial year ended 31.12.2005	<u>34,50,000</u>
TOTAL	<u>66,00,000</u>
Average of net profits during three preceding financial years	<u>22,00,000</u>
Five per cent thereof	<u>1,10,000</u>

Since this amount is higher than Rs.50,000/-, the Board of Directors of PTL Ltd. can

make contribution to charitable funds upto Rs.1,10,000/- during the financial year 2005-06 without obtaining the approval of shareholders in a general meeting.

Question 18

Examine the validity of the resolution passed at the Annual General Meeting of a public company for payment of dividend at a rate higher than that recommended by the board of directors. Is it possible for the board of directors of the company to revoke the dividend declared at the Annual General Meeting?

The Board of Directors of XYZ Limited having paid-up share capital of ₹ 6 crores and free reserves of Rs.3 crores proposes to increase the sitting fee which is at present Rs.5,000. They seek your advice about the maximum amount upto which the sitting fee may be increased without seeking the approval of the Central Government. Advise explaining the relevant provisions of the Companies Act, 1956. (CA Final, New Course, November, 2008)

Answer

According to Regulation 85 of Table A of the Companies Act, 1956, a company in general meeting may declare dividends, but no dividend shall exceed the amount recommended by the Board of Directors of the company. The shareholders at an Annual General Meeting may reduce the amount of dividend recommended by the Board of Directors of the company, but they cannot increase it. Hence the resolution passed at the Annual General Meeting for payment of dividend at a rate higher than that recommended by the Board of Directors is not valid.

Revocation of declared dividend

Ordinarily, a dividend once declared at Annual General Meeting, cannot be revoked, except, with the consent of the shareholders, for a declaration of dividend creates a debt to the shareholders in whose favour it is declared. If a dividend is declared and the amount is paid or credited to the shareholders as dividend, the character of the credit or payment as dividend cannot be altered by a subsequent resolution (*Kishanchand Chellaram VCIT (1962) 32 Company cases 1046,105C (SC)*).

But where a dividend has been illegally declared, or where, due to events intervening — after the declaration, such as fire destroying the company's property, or the out break of a war, or the composition of new heavy tax burden or other causes diminishing the assets of the company makes it advisable to conserve the remaining assets, the Board of Directors will be justified in revoking the declaration of dividend.

Sitting fees

The company proposes to increase the Sitting fees payable to directors for attending Board meetings without seeking the approval of the Central Government for such increase. According to the first provision to Section 310 of the Companies Act, 1956, any increase in sitting fees up to prescribed limit will not require approval of the Central Government. As per

12.18 Corporate and Allied Laws

rule 10b of Companies (Central Governments) General Rules & Forms, 1956 maximum sitting fees payable per meeting of Board of Directors or its committee is as follows-

- (a) Rs.20,000 per meeting if paid up capital plus free reserves are Rs.10 crore or more or turnover is Rs.50 crore or more (since word used is "or", it is so sufficient if one of the conditions is satisfied).
- (b) ₹ 10,000 per meeting in other cases (i.e. company whose paid up capital plus free reserves is less than Rs.10 crore and turnover is less than Rs.50 crore).

The paid up capital plus free reserves of XYZ Ltd is less than ₹ 10 crore and information regarding turnover is not available. If the turnover of the company is also less than Rs.50 crore, the Sitting fees can be increased only up to Rs.10,000 per meeting ,without seeking approval of the Central Government. If the turnover is Rs.50 crore or above Sitting fees can be increased up to Rs.20,000 without approval of the Central Government.

Question 19

Big Ben Ltd., a reputed public company, had advanced certain sum of money to one of its Directors, namely, Mr. Tanmay on certain terms and conditions and fixing the time limit for repayment thereof. Now, Mr. Tanmay has approached the Company with a request to extend the time limit for repayment of balance of loan amounting to Rs.12.00 lacs by another six months.

You are required to state with reference to the provisions of the Companies Act, 1956, the answer to the following:

- (i) *Who is authorized to grant the extension as requested by Mr. Tanmay?*
- (ii) *Draft an appropriate notice for the meeting where such extension may be granted.*

(CA Final, New Course, June 2009)

Answer

- (i) As per provisions of Section 293(1)(b) of the Companies Act, 1956, the Board of Directors of Big Ben Ltd., a public company can not give time for the repayment of any debt due by Mr. Tanmay, a director of the company except with the consent of the Company by way of an ordinary resolution passed in a General Meeting. In view of this provision of the law, the Company in a General Meeting is authorized to grant the extension as requested by Mr. Tanmay.
- (ii) Notice for calling the General Meeting of the company:

BIG BEN LIMITED

Registered Office: _____

NOTICE FOR EXTRA ORDINARY GENERAL MEETING

NOTICE is hereby given that an Extra Ordinary General Meeting of the members of the company will be held at the Registered office of the Company on _____,

Board's Powers and Restrictions Thereon (Sections 291 – 293) 12.19

the _____ day of _____, 2009 at 11.00 A.M. to transact the following business:

- (1) To pass, with or without modification, the following resolution as an Ordinary Resolution:

“RESOLVED THAT pursuant to the provision of Section 293(1)(b) of the Companies Act, 1956, consent be and is hereby accorded to the company for extending the time for the repayment of the balance amount of ₹ 12.00 Lacs advanced to Mr. Tanmay, a Director of the company, by a further period of six months ending on _____, 2009.”

FOR & ON BEHALF OF THE BOARD

Dated. _____, 2009 _____

Company Secretary _____

Notes:

- (1) A member entitled to attend and vote at the Meeting is entitled to appoint a proxy to attend and vote instead of himself and such proxy need not be a member of the Company. Proxies in order to be valid must be deposited at least 48 hours prior to commencement of the Meeting.
- (2) Explanatory Statement pursuant to Section 173(2) of the companies Act, 1956 is annexed hereto

Question 20

The Board of Directors of LM Limited propose to donate Rs.3,00,000 to a school established exclusively for the benefit of children of employees and also donate Rs.50,000 to a political party during the Financial year ending 31st March, 2010. The average net profits determined in accordance with the provisions of Sections 349 and 350 of Companies Act, 1956 during the three immediately preceding financial years is Rs.40,00,000. Examine with reference to the provisions of the Companies Act, 1956 whether the proposed donations are within the power of the Board of Directors of company. **(CA Final, New Course, June 2009)**

Answer

Donations: As per section 293(1) (e) of the Companies Act, 1956, the Board of Directors of a Company must obtain approval of the shareholder by way of resolution passed in their meeting for contributing in any year, to charitable and other funds not directly relating to the business of the company or the welfare of to employees any amount exceeding Rs.50,000 or 5% of its average net profits of the last 3 financial years, whichever ever higher. In the given case, the school is established exclusively for the benefit of the children of the employees of the company and hence the restriction under section 293 (1) (e) is not applicable and the Board is empowered to make the proposed donation.

12.20 Corporate and Allied Laws

Donation to political parties: It is presumed that LM Ltd is not a Government Company. It has been in existence for more than 3 years. The proposed donation to a political party is only Rs.50,000 which is less than 5% of the average net profit for 3 immediately preceding financial years. Hence the Board of Directors is empowered to make a donation by passing a resolution at a Board meeting. The company is also required to make is proper disclosure in the profit and loss account. (Section 293 A).