

MOCK TEST PAPER – 1

FINAL COURSE: GROUP – I

PAPER – 4 : CORPORATE AND ALLIED LAWS

SUGGESTED ANSWERS/HINTS

1. (a) **Increase in the number of directors:** As per Section 259 of the Companies Act, 1956 in the case of a company incorporated after 21st July, 1951 any increase in the number of its Directors beyond the maximum fixed by its Articles of Association as originally adopted and registered in the case of a company existing prior to that date, any increase in the number of Directors shall not have any effect unless approved by the Central Government. However, such approval from the Central Government is not required if the number of Directors is increased to 12 or less than that. The above mentioned provisions of Section 259 of the Companies Act, 1956 are applicable only to public companies or private companies which are subsidiaries of public companies.

In view of the above, since Rajasthan Toys Private Limited is a private company and it is also not subsidiary of any public company, the provisions of Section 259 of the Companies Act, 1956 are not applicable and the Board of Directors of the said company may increase the number of Directors without seeking approval of the Central Government.

- (b) Notice of every Board meeting has to be served in writing on each director for the time being in India, and at his usual address in India to every other director. Every officer of the company whose duty is to serve the notice as aforesaid and who fails to do so shall be punishable with fine extending to ₹ 1000 (Section 286). It is usually the secretary of the company on whom it casts the duty to serve the notice as aforesaid. It should be noted that the company is not liable for the default in the service of the said notice; it is only the officer in default who is subject to the said penalty. Although there is no legal precedence in this regard, it would be a prudent practice on strictly construing Section 286 that the notice should be served to the alternate director as well as on the original director who is outside India for the time being.
- (c) **Transfer of certain duties and functions of a clearing house by a stock exchange to clearing corporation under the Securities Contracts (Regulation) Act, 1956 (Section 8A)**

Purposes:

A recognized stock exchange may, with the prior approval of the Securities and Exchange Board of India, transfer the duties and functions of a clearing house to a

clearing corporation, being a company incorporated under the Companies Act, 1956 for the purpose of:

- (i) the periodical settlement of contracts and differences thereunder,
- (ii) the delivery of, and payments for, securities;
- (iii) any other matter incidental to, or connected with, such transfer.

Procedure:

1. Every clearing corporation shall for the purpose of transfer of the duties and functions of a clearing house to clearing corporation make bye-laws and submit the same to the SEBI for approval.
 2. The SEBI may, on being satisfied that it is in the interest of the trade and also in the public interest to transfer the duties and functions of a clearing house to a clearing corporation, grant approval to the bye-laws submitted to it under sub-section (2) and approve transfer of the duties and functions of a clearing house to a clearing corporation.
 3. The provisions of Sections 4 to 12 shall, as far as may be, apply to a clearing corporation as they apply in relation to a recognized stock exchange.
- (d) Where the Profit and Loss Account and the Balance sheet of the company do not comply with the Accounting Standards read with Schedule VI and Section 211 of the Companies Act, 1956, such companies shall disclose in its Profit and Loss account and Balance Sheet, the following:
- (i) the deviation from the accounting standards.
 - (ii) the reasons for such deviations; and
 - (iii) the financial effect, if any, arising due to such deviation.

If any such person as is referred to in sub-section (6) of Section 209 fails to take all reasonable steps to secure compliance by the company, as respects any accounts laid before the company in general meeting, with the provisions of this section and with the other requirements of this Act as to the matters to be stated in the accounts, he shall, in respect of each offence, be punishable with imprisonment for a term which may extend to 6 months, or with fine which extend to ₹ 10,000 or with both.

2. (a) As per section 399 of the Companies Act, 1956, in the case of a company having a share capital, members eligible to apply for oppression and mismanagement shall be lowest of the following:

100 members; or

1/10th of the total number of members; or

Members (including equity shareholder as well as preference shareholder) holding not less than 1/10th of the issued share capital of the company.

The consent to be given by shareholder is reckoned at the beginning of the proceedings. The withdrawal of consent by shareholder during the course of proceedings does not affect the maintainability of the application.

In the question above, the shareholding pattern of the company is as follows:

₹ 9,00,000 equity share capital held by 600 members.

₹ 1,00,000 preference share capital held by 5,000 members.

₹ 10,00,000 total share capital held by 5,600 members.

The application alleging oppression and mismanagement has been made by the members as follows:

(i) Number of members making the application:

- Preference shareholders 400
- Equity shareholders 50
- Total members 450

(ii) Amount of share capital held by members making the application:

- Preference share capital ₹ 4,00,000 (400 preference shares of ₹10 each)
- Equity share capital ₹ 5,00,000 (500 equity shares of ₹10 each)
- Total capital ₹ 9,00,000

The application shall be valid if it has been made by the lowest of the following:

100 members

560 members (being 1/10th of 5,600)

Members holding ₹1,00,000 share capital (being 1/10th of ₹10,00,000)

As it is evident, the application made by 450 members meets the eligibility criteria specified u/s 399; therefore, the application is maintainable.

Such application shall remain valid despite the fact that some of the applicants have withdrawn their consent.

(b) EXTENSION OF FINANCIAL YEAR:

Where it appears to the Central Government that it is desirable for a holding company or a holding company's subsidiary to extend its financial year so that the subsidiary's financial year may end with that of the holding company, and for that purpose to postpone the submission of the relevant accounts to a general meeting, the Central Government may on the application or with the consent of the Board of

Directors of the company whose financial year is to be extended, direct that in the case that company the submission of accounts to a general meeting, the holding of an annual general meeting or the making of an annual return, shall not be required to be submitted or made, earlier than the dates specified in the direction not withstanding anything to the contrary in the Companies Act, 1956 or in any other Act for the time being in force.

Thus the management can extend the financial year of Sunrise Limited from 12 months to 21 months.

Following steps are required to be taken for this purpose.

1. To convene a meeting of the Board of Directors of Sunrise Limited whereat the resolution for extending the financial year is to be passed so that the year ending matches with the year ending of Hotline Ltd.
2. To make an application under Section 213 of the Companies Act, 1956 to the Central Government giving full details and specific reasons for seeking the extension in year ending.
3. To attach the following to the application:-
 - (i) A certified copy of the Last Balance Sheet and Profit & Loss Account of Hot Line Limited and Sunrise Limited.
 - (ii) A certified copy of the Memorandum of Association and Articles of association of both the companies.
 - (iii) A certified copy of the resolution of the Board of Directors proposing the extension of the financial year.
 - (iv) Requisite fee payable to the Central Government under Rules.
3. (a) Under Section 310 of the Companies Act, 1956 approval of the Central Government shall not be required where sitting fee for each meeting of the Board of a Committee thereof does not exceed the prescribed sum under Rule 10-B of the Central Government's (General Rules & Forms, 1956) as under:

1.	Companies with paid up capital of ₹ 10 crores and above or turnover of ₹ 50 crores and above	Sitting fee not to exceed ₹ 20,000
2.	Other companies	Sitting fee not to exceed ₹ 10,000

Any increase in the sitting fee will require amendment of relevant provision of the Articles of Association. In the given case, the proposed sitting fee of ₹ 25,000 will require approval of the Central Government as the same exceeds the prescribed limits. The company can pay the sitting fee upto ₹ 20,000 depending upon the aforesaid parameters laid down in Rule 10-B.

(b) Retiring director – When to be deemed director?

In accordance with the provision of the Companies Act, 1956, as contained in Section 256(3) at the annual general meeting at which a director retires as aforesaid, the company may fill up the vacancy by re-appointing the retiring director or some other person thereto. If the place of retiring director is not so filled up and the meeting has not expressly resolved not to fill the vacancy, the meeting shall stand adjourned to same day in the next week, at the same time and place, or if that day is a public holiday, till the next succeeding day which is not a public holiday. If at the adjourned meeting also, the place of the retiring is not filled up and that meeting also has not expressly resolved not to fill the vacancy, the retiring director shall be deemed to have been re-appointed at the adjourned meeting, unless at the adjourned meeting or at the previous meeting a resolution for the re-appointment of such directors was put and lost.

Therefore, in the given circumstances answer to the questions as asked shall be:

- (i) In the first case, applying the above provisions, the retiring directors shall be deemed to have been re-appointed.
- (ii) In the second case, where the resolutions were lost, the retiring directors shall not be deemed to have been re-appointed.
- (iii) In the third case the directors due to retire shall vacate their offices latest on the date on which Annual General Meeting was to be held. (*B.R. Kundra v. Motion Pictures Association, 1976, 46 Comp. Cas. 339*)

4. (a) (i) Proceedings of Annual General Meeting not held in time

Failure to hold annual general meeting within the time prescribed under section 166 of the Companies Act, 1956 is an offence punishable under section 168. Thus, if a meeting is held beyond due date, it only involved penalty and it is not void meeting. All the resolution passed in such a meeting are valid.

(ii) Appointment of a proxy by a person representing a member company.

According to Section 187 (2) of the Companies Act, 1956 a person authorized by board resolution of a member company shall be entitled to exercise the same rights and powers (including the rights to vote by proxy) on behalf of the body corporate which he represents as that body could exercise if it were an individual member. The representative may, instead of being present in person, appoint a proxy.

(iii) Fresh proxies for adjourned general meeting

A proxy properly lodged before a general meeting will be valid for an adjourned meeting also. It is also possible to lodge fresh proxies 48 hours before the adjourned meeting is held. Regulation 61 of Table A specifically permits

deposit of proxies 48 hours before the time for holding the adjourned meeting. Companies may adopt Table A or its articles may contain provisions similar to Regulation 61. Hence fresh proxies deposited in time for the adjourned meeting are valid.

(iv) Casting vote in respect of a special resolution

Regulation 54 of Table A provides for casting vote by the chairman of a general meeting in case of equality of votes. Companies usually provide for similar provision on the articles. However in absence of specific provision, chairman does not have a casting vote. Further, Chairman can use his casting vote only when there is equality of votes. Thus, the vote can be used only for ordinary resolution and not where a special resolution is required.

- (b)** Section 530 of the Companies Act, 1956 lays down the procedure for payment of debts out of available funds with the Official Liquidator. However, Section 529A provides for overriding of the preferential payments as mentioned in Section 530. According to Section 529A, notwithstanding anything contained in other provisions of this Act or any other law for the time being in force, in the winding up of a company,

- (i) workmen's dues; and
- (ii) debts due to secured creditors, shall be paid in priority to all other debts.

The above debts have to be paid in full unless the assets are insufficient to meet them, in which case they shall abate in equal proportions.

In this light of the legal provisions explained, the funds available with the Official Liquidator are not even sufficient to meet fully the dues payable to secured creditors and workers. Thus, tax dues to the tune of ₹ 4,00,000 payable to Government authorities will not get any payment even though they are to be considered as preferential payments as per section 530 of the Act. The secured creditors dues and workmen dues will get abated equally and they get ₹ 32 lakhs and ₹ 24 lakhs respectively. The other creditors will get nothing.

5. **(a)** (i) Section 224(5) of the Companies Act, 1956 lays down that the first auditor of a company shall be appointed by the Board of Directors within one month of the date of registration of the company.

If the Board of Directors fails to exercise its power, the company in general meeting may appoint the first Auditor or Auditors.

Subsequently Auditor or Auditors of a company are appointed every year by the shareholders in annual general meeting by passing an ordinary resolution.

- (ii) Auditor appointed in an Annual General Meeting may be removed from office before the expiry of his term only by the company in general meeting, after obtaining the previous approval from the Central Government in that behalf [Section 224 (7)].

Further the company has to follow the following procedure prescribed in Section 225 (2) and (3) as explained below:

No special notice under section 225 (1) is required for a resolution in the general meeting to remove the auditor, hold the general meeting etc.

The auditor shall be informed of the Board's decision immediately. [Section 225 (2)].

The auditor can make a representation. The copy of the representation should be sent to all the members to whom notice of meeting is sent. If the copy of the representation is not sent as it was received late or because of the company's fault, the auditor may insist that the representation may be read at the meeting. [Section 225 (3)].

If company does not wish to send the representation to the members or read at the general meeting, the company has to apply to Central Government/Company Law Board. If Central Government/Company Law Board is satisfied that the right of representation is being misused by auditor to secure needless publicity for defamatory matter, the Central Government/Company Law Board may order that the representation need not be sent and the representation need not be read at the meeting. (Proviso to Section 225(3)).

An ordinary resolution is to be passed at the general meeting for the removal of the auditor.

The first auditors appointed by Board can be removed by the company at a general meeting. (Proviso (a) to Section 224 (5)). The provisions in respect of removal as contained in Section 225 (2) & (3) are applicable for removal of first auditors also. (Section 225 (4)). However, in case of removal of first auditor appointed by the Board of Directors, only an ordinary resolution is sufficient to remove the auditor and Central Government's approval is not required.

- (b) Regulation 26 of the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 prescribes the conditions to be fulfilled for issue of shares. As per the said Regulation, an issuer may make an initial public offer, if:
- (i) it has net tangible assets of at least three crore rupees in each of the preceding three full years (of twelve months each), of which not more than fifty per cent are held in monetary assets. Further that if more than fifty per cent of the net tangible assets are held in monetary assets, the issuer has made firm commitments to utilise such excess monetary assets in its business or project.
 - (ii) it has a track record of distributable profits in terms of section 205 of the Companies Act, 1956, for at least three out of the immediately preceding five years. The extraordinary items shall not be considered for calculating

distributable profits.

- (iii) it has a net worth of at least one crore rupees in each of the preceding three full years (of twelve months each).
- (iv) the aggregate of the proposed issue and all previous issues made in the same financial year in terms of issue size does not exceed five times its pre-issue net worth as per the audited balance sheet of the preceding financial year.
- (v) if it has changed its name within the last one year, at least fifty per cent. of the revenue for the preceding one full year has been earned by it from the activity indicated by the new name.

In the given case,

- (i) The net tangible assets of the company as per the last three audited balance sheets as on 31st March, 2007, 2008 and 2009 were ₹ 4.00 crores, ₹ 4.50 crores, and ₹ 5.00 crores respectively. It satisfies the requirements of clause (a) as above as during each of the preceding three full years, it has net tangible assets, more than ₹3 crores and out of which the monetary assets are not more than 50 % of the net tangible assets. (In this case it has monetary assets less than Rs 50 lacs).
- (ii) The company has good track record of distributable profits in terms of section 205 of the Companies Act, 1956. In other words, it has not incurred any loss in any year in the past.
- (iii) The net worth of the company during the three preceding years was at least ₹ 1 crore in the preceding three full years. (paid-up capital since 1st April, 2001 is Rs 3 crores and net worth as at 31st March, 2007 was ₹ 5.00 crores).
- (iv) The aggregate of the proposed issue and all previous issues made in the same financial years does not exceed 5 times its pre-issue net worth. (₹ 20 crores is the proposed issue and pre-issue net worth is ₹ 5 crores as on 31st March, 2009).
- (v) It is stated in the problem that the revenue earned by the company under its activity (chemical) the new name is more than from the old activity (engineering, it satisfied the condition (e) as stated above.

Hence Chirag Chemicals & Engineering Ltd can proceed to make a public issue of shares to raise ₹ 20.00 crores by issuing equity shares at premium.

6. (a) Every Banking Company incorporated in India must create a Reserve Fund and transfer a sum equal to not less than 20 % of its net profits (Section 17). However, Central Government is empowered to exempt from this requirement on the recommendation of the RBI. Such exemption will be allowed only:-

- when the amounts in the reserve fund and the share premium account are equal to the paid-up capital of the banking company
- when the Central Govt. feel that its paid-up capital and reserves are adequate to safe guard the interest of the depositors

If a banking company appropriates any sum from the Reserve fund or the share premium account, it must be reported to RBI within 21 days explaining the circumstances leading to such appropriation

(b) Director Identification Number: It is an unique Identification Number allotted to an individual who is an existing director of a company or intends to be appointed as director of a company pursuant to section 266A & 266B of the Companies Act, 1956 (as amended vide Act No 23 of 2006).

A provisional DIN is approved only after scrutiny of the documents attached with the application. Some of the common mistakes committed by applicants and on account of which the DIN application gets rejected are as under: - Non payment of DIN application fee.

- The DIN application fee is not paid

Non-submission of supporting documents

- The proof of identity of the applicant is not submitted.
- The proof of father's name of the applicant is not submitted.
- The proof of date of birth of the applicant is not submitted.
- The proof of residential address of the applicant is not submitted.
- The Affidavit (for applicant or his/her father's name being a single name) is not submitted.
- The copy of passport (for foreign nationals) is not submitted

Invalid Application/supporting Documents

- The supporting documents are invalid or expired.
- The proof of identity submitted has not been issued by a Government Agency.
- The application/enclosed evidence has handwritten entries.
- The submitted application is a duplicate DIN application and already one application of that applicant is pending or approved.
- The submitted application does not have photograph affixed.
- The signatures are not appended to the prescribed place.
- The applicant's name filled in application form does not match with the name in the enclosed evidence.

- The applicant's father's name filled in application form does not match with the father's name in the enclosed evidence.
- The applicant's date (DD/MM/YY) of birth filled in application form does not match with the date of birth in the enclosed evidence.
- The address details filled in the application do not match with those contained in the enclosed supporting evidence.
- The prefixes/ suffixes like Mr. / Ms. / Kumari / Shri / Late/Ji etc. are used in the applicant's name or applicant's father's name field in Form DIN-1.
- The gender is not entered correctly in Form DIN-1.
- Identification number entered in application does not match with the identity proof enclosed.
- The application does not contain the valid Service Request Number (SRN) through which the DIN application fee is paid.

Improper Attestation of documents

- The attesting authority has not put his signature.
- The documents have not been attested by authorized person.
- Applicant's photograph has not been attested by an authorized person.
- The proof of identity has not been attested by an authorized person.
- The proof of father's name has not been attested by an authorized person.
- The proof of date of birth of the applicant has not been attested by an authorized person.
- The proof of residential address has not been attested by an authorized person.
- The particulars of the attesting authority are incomplete (e.g. professional's name, designation, membership number, stamp/seal).

7. (a) Person resident in India (Foreign Exchange Management Act, 1999):

- (i) Any person or body corporate registered or incorporated body in India is a resident in India [section 2(v)(ii)]. 'Person' includes a company [section 2(u)]. An office, branches or agency outside India owned or controlled by a person resident in India is a person resident in India. [Section 2(v)(iv)].

In view of the above provisions in FEMA, 1999 London branch established by ABC Ltd, a company incorporated in India, is a 'person resident in India' under the Act from the date of establishment i.e. 1st January, 2010.

- (ii) According to Section 2(v)(iii) of FEMA, 1999 an office, branch or agency in India owned or controlled by a person resident outside India is a person

resident in India'. Only a body corporate registered or incorporated in India is a 'person resident in India'. According to section 2(w), 'person resident outside India' means a person who is not resident in India. Hence M/s XYZ, foreign company is a 'resident outside India. But the branch at New Delhi owned by M/s XYZ is a 'resident in India' within the meaning of section 2(v) (iii) from the date of establishment i.e. 1st January, 2010. The branch at Colombo controlled by the branch at New Delhi referred to in the question is a person 'resident in India' within the meaning of section 2(v)(iii) read with section 2(v)(iv).

- (b) Provisions of Section 11(2) of the Competition Act, 2002 empower the Central Government to remove, by an order, a member of the Competition Commission of India from his office if such member has acquired such financial interest as is likely to affect prejudicially his functions as a Member of the Competition Commission. However, provisions of Section 11(3) of the said Act put some restrictions on such powers of the Central Government. According to this section, in case as stated in the question, the Central Government wants to remove a member of the Competition Commission from his office, it has to make a reference to the Supreme Court. The Supreme Court shall hold an enquiry in accordance with the procedure formulated by it and then report that the member in question ought to be removed from his office.

Thus, the Central Government can remove a member of Competition Commission from his office by following the above procedure.

- (c) As per Section 581J of the Companies Act, 1956, any Inter-State Co-operative Society with objects not confined to one State may make an application to the Registrar of Companies for registration as Producer Company.

The application for registration as a producer Company is to be submitted along with the following:

- (i) a copy of the special resolution, of not less than two-third of total members of Inter-State Co-operative Society, for its incorporation as a Producer Company under the Companies Act:
- (ii) a statement showing:
 - (a) Names and addresses or the occupation of the directors and Chief Executive, if any, by whatever name called, of such inter-State Co-operative Society, and
 - (b) list of members of such Inter-State Co-operative Society;
- (iii) a statement indicating that the Inter-State Co-operative Society is engaged in any one or more of the objects specified in Section 581B of the Companies Act, 1956;
- (iv) a declaration by two or more directors of the Inter-state co-operative society certifying that particulars given in the above statements are correct.

- (d) When particular words pertaining to a class or genus are followed by general words, the general words are construed as limited to things of the same kind as those specified. This rule which is known as Rule of ejusdem generis reflects an attempt 'to reconcile incompatibility between the specie and general words in view of the other rules of interpretation that all words in the statute are given effect if possible, that a statute is to be construed as a whole and that no words are presumed to be superfluous. For instance, where an Act permits keeping of dogs, cats, cows, buffaloes and other animals the expression 'Other animals' would not include animals like lions and tigers, but would mean, only domesticated animals like horses etc.

The rule applied when (i) the statute contains an enumeration of specific words: (ii) the subjects of enumeration constitute a class or category: (iii) that class or category is not exhausted by the enumeration; (iv) the general terms follow the enumeration; and (v) there is no indication of a different legislative intent. If the subjects of enumeration belong to a broad based genus as also to narrower genus, there is no principle that the general words should be confined to the narrower genus.

The rule is applied extensively in interpreting the various statutes. The rule of ejusdem generis has to be applied with care and caution. It is not an inviolable rule of law, but only permissible reference in the absence of an indication, to the contrary, and where the context and the object and mischief of the enactment do not require restricted meaning to be attached to word of general import, it becomes the duty of the courts to give words their plain and ordinary meaning. The rule of ejusdem generis has no inverse application. General words preceding the enumeration of specific instances are not governed by this rule and their import cannot be limited by such words.

- (e) **Enforcement of Security interest under SARFAESI Act, 2002 Section 13):** Notwithstanding anything contained in section 69 or section 69A of the Transfer of Property Act, 1882 (4 of 1882), any security interest created in favour of any secured creditor may be enforced, without the intervention of the court or tribunal, by such creditor in accordance with the provisions of this Act.

Where any borrower, who is under a liability to a secured creditor under a security agreement, makes any default in repayment of secured debt or any installment thereof, and his account in respect of such debt is classified by the secured creditor as on-performing asset, then, the secured creditor may require the borrower by notice in writing to discharge in full his liabilities to the secured creditor within sixty days from the date of notice failing which the secured creditor shall be entitled to exercise all or any of the rights under sub-section (4) of Section 13. This notice shall give details of the amount payable by the borrower and the secured assets intended to be enforced by the secured creditor in the event of non-payment of secured debts

by the borrower. The procedure for the service of the notice is prescribed in the Security Interests (Enforcement) Rules.

Sub-section (4) of Section 13 provides that if the borrower fails to discharge his liability in full within the above specified period, the secured creditor may take recourse to one or more of the following measures to recover his secured debt:-

- (i) take possession of the secured assets of the borrower including the right to transfer by way of lease, assignment or sale for realising the secured asset;
- (ii) take over the management of the secured assets of the borrower including the right to transfer by way of lease, assignment or sale and realise the secured asset;
- (iii) appoint any person (hereafter referred to as the manager), to manage the secured assets the possession of which has been taken over by the secured creditor;
- (iv) require at any time by notice in writing, any person who has acquired any of the secured assets from the borrower and from whom any money is due or may become due to the borrower, to pay the secured creditor, so much of the money as is sufficient to pay the secured debt.

any beneficial interest in property, whether movable or immovable or in such debt, receivables, whether such interest is existing, future accruing, conditional or contingent; or any financial assistance. (Section 2(1)).