

MOCK TEST PAPER – 2

FINAL COURSE: GROUP – I

PAPER – 4 : CORPORATE AND ALLIED LAWS

SUGGESTED ANSWERS/HINTS

- 1 (a) **Right to carry out the inspection of the books of accounts:** Mr. A has no right to carry out an inspection of the books of accounts of the company despite the fact that he holds 51% of the share capital of the company and can be called the 'owner' of the company. According to Sections 209 and 209A of the Companies Act, 1956, the following persons have the right to carry out the inspection of the books of accounts of the company.
- (i) Directors of the Company [Section 209(4)]
 - (ii) Registrar of Companies [Section 209A]
 - (iii) Such officer of Government as may be authorised by the Central Government in this behalf (Section 209 A).
 - (iv) Such officers of SEBI as may be authorised by SEBI [Section 209A (1) (iii)] read with Section 55A.

Since Mr. A is not a director, he is not eligible to carry out the inspection.

Note: According to Regulation 95, of Table A, Companies Act, 1956, a member has right to inspect the books of accounts if he is so authorized by a resolution of the Board of Director or a resolution passed by the company in general meeting. According to this, the members have right to inspect the books of account.

- (b) Section 262 of the Companies Act, 1956 authorises the Board of Directors to fill up casual vacancies if the office of any director appointed by the company in general meeting is vacated before his term of office and hence the appointment of C was in order. In normal course, C could have held his office as director up to the date to which Mr. P would have held but Mr. C expired on 15th May 2009 and again a vacancy has arisen in the office of director owing to death of Mr. C who was appointed by the board to fill up the casual vacancy.

Hence the present vacancy cannot be considered as casual vacancy as stated in section 262 and therefore the board cannot fill up the same.

The Board may however appoint Mrs. C as an additional director under section 260 of the Act provided the articles of association authorises the board to do so, in which case Mrs. C will hold the office until the conclusion of the next annual general meeting.

- (c) Under section 22A of the Securities Contracts (Regulation) Act, 1956 where a recognised Stock Exchange refuses to list the securities of any public company, the company shall be entitled to be furnished with reasons for such refusal. If aggrieved, the company may appeal to the Securities Appellate Tribunal:
- (i) within 15 days from the date on which the reasons for such refusal are furnished to it, or
 - (ii) where the Stock Exchange has omitted or failed to dispose of within the time specified in section 73(1A) of the Companies Act, 1956 (i.e., before the expiry of ten weeks from the date of closing of the subscription list as per prospectus) within 15 days from the expiry of the specified time or within such further period not exceeding one month as Securities Appellate Tribunal may allow.

In terms of section 22E of the Act, Civil Court has no jurisdiction to entertain any suit in respect of this matter.

The company may be advised accordingly.

- (d) **Investor Education & Protection Fund:** Any money transferred to the unpaid dividend account of a company in pursuance of section 205A of the Companies Act, 1956, which remains unpaid or unclaimed for a period of seven years from the date of such transfer shall be transferred by the company to the Investor Education and Protection Fund established under sub-section (1) of section 205C.

According to Section 205C of the said Act, the following amounts shall be credited to the Fund:

- (a) amounts in the unpaid dividend accounts of companies;
- (b) the application moneys received by companies for allotment of any securities and due for refund;
- (c) matured deposits with companies;
- (d) matured debentures with companies;
- (e) the interest accrued on the amounts referred to in (a) to (d) as above;
- (f) grants and donations given to the Fund by the Central Government, State Governments, companies or any other institutions for the purposes of the Fund; and
- (g) the interest or other income received out of the investments made from the Fund.

No such amounts referred to in clauses (a) to (d) shall form part of the Fund unless such amounts have remained unclaimed and unpaid for a period of seven years from the date they became due for payment.

- 2 (a) **RECONSTRUCTION SCHEME OF COMPANY:** The provisions contained in sections 391 to 394 of the Companies Act, 1956 are applicable to Wagonbound Limited as it can be considered as a company liable to be wound up within the meaning of Section 390 of the Companies Act, 1956. The proposed scheme involves a compromise or arrangement with members and creditors and it attracts section 391 of the said Act.

While the company or any creditor or member can make application to the Court/Tribunal under Section 391, it is usual for the company to make an application. On such application the Court/Tribunal may order that a meeting of creditors and/or members be called and held as per the directions of the Court/Tribunal.

The company must send notice of meeting to every creditor/member containing a statement setting forth the terms of compromise or arrangement explaining its effect. Material interest of directors, Managing Director or manager of the company in the scheme and the effect of scheme on their interest should be fully disclosed (Section 393). At the meetings convened as per directions of the Court/Tribunal majority in number representing at least $\frac{3}{4}$ in value of creditors/members present and voting must agree to compromise or arrangement. Thereafter the company must present a petition to the Court/Tribunal for confirmation of the compromise or arrangement.

The notice of application made by the company will be served on the Central Government and the Tribunal will take into consideration representation, if any, made by the Central Government (Section 394A). The Court/Tribunal will sanction the scheme, if satisfied, after considering all relevant matters.

Copy of order issued by the Court/Tribunal must be filed with the Registrar of Companies and then only the order will come into effect. Copy of the said order must be annexed to every Memorandum of Association issued thereafter. The scheme sanctioned by the Court/Tribunal shall be binding on all members and creditors even those who were dissenting.

Note: The power under the scheme of reconstruction etc. is still with the High Courts pending constitution of the National Company Law Tribunal.

- (b) (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:

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.

- 3 (a)** The matter of appointment of directors at the general meeting has been correctly stated in the agenda as the ordinary business to be transacted at the general meeting. But in accordance with the provisions of the Companies Act, 1956 as contained in Section 263 at a general meeting of a public company or of a private company which is a subsidiary of a public company, a motion shall not be made for the appointment of two or more persons as directors of the company by a single resolution unless a resolution that it shall be so made has first been agreed to by the meeting without any vote being given against it. Any resolution moved in contravention of sub-section (1) shall be void, whether or not objection was taken at

the time to its being so moved. However, Government and companies incorporated under Section 25, i.e. associations not for profit have been exempted from the above.

Answer to Problems:

1. Taking into account the above, the contention of the members shall be tenable. Each director has to be appointed by way of a separate resolution.
2. In the second case since the company is an association not for profit under section 25 of the Companies Act, 1956 the above provisions do not apply.

(b) 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.

- 4 (a) (i) There is no difficulty at all in holding the board meeting at Chennai even if all the directors of the company reside at Kolkata and the registered office is situated at Kolkata provided requirements regarding signing of register of contracts, etc. are complied with.
- (ii) Under provisions of Section 166 of the Companies Act, 1956, the annual general meeting shall be held during business hours and on a day that is not a public holiday. There is no similar provision in the Act with regard to board meetings. Therefore, in the absence of any specific restrictive provision, the board meeting can be held even on a public holiday and out of the business hours. The term “public holiday” in this context should be understood. According to the proviso to Section 2 (38) no day declared by the Central

Government to be a public holiday shall be deemed to be a public holiday unless the declaration was notified before the issue of the notice of the meeting. Suppose, the notice of a meeting was issued on April 1st where by it was to be held on May 3. If on April 2, the Central Government declares the 3rd day of May as a public holiday, there is no bar to the holding of the meeting on May 3 in spite of its being declared as a public holiday. If, however, the declaration is notified before the issue of the notice convening the meeting, say on 31st March, the meeting cannot be held on May 3.

- (iii) If the articles of association of the company are silent, the notice of board meeting is not required to specify the nature of business to be transacted thereat [*Compagnie de Mayville v. Whitley (1896) 1 Ch. 788 (CA)*]. If, however, the articles provide otherwise, then the notice must specify the nature of business to be transacted. All said and done, a better course seems to be that the notice should specify the purpose of the meeting, if it is an extra-ordinary or special meeting.
- (b) Section 398 of the Companies Act, 1956 provides that a requisite number of members of the company as laid down in Section 399 may apply to Company Law Board for appropriate relief on the ground of mismanagement of the company.

Conditions Precedent:

Section 398 can be invoked in either of the two circumstances:

- (a) that affairs of the company are being conducted in a manner prejudicial to the interests of the company [Section 398(1)(a)]; or
- (b) that a material change has taken place in the management or control of the company and as a consequence the affairs of the company may be conducted in a manner prejudicial to the public interest or in a manner prejudicial to the interests of the company [Section 398(1)(b)].

Considering the above, the questions as asked can be answered as under:

1. Continuation of directors in their office after the expiry of their term and infighting among them has been held to be the act of mismanagement. (*Ranjan Dutta vs. Bholu Nath Paper House Ltd. (1983)*).
 2. Non-declaration of dividend when it does not lead to devaluation of shares is not an act of mismanagement. (*V.J. Thomas Vettom vs. Kuttanad Rubber Co. Ltd. (1984)*).
- 5 (a) **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 notwithstanding 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:-
 - (a) A certified copy of the Last Balance Sheet and Profit & Loss Account of Hot Line Limited and Sunrise Limited.
 - (b) A certified copy of the Memorandum of Association and Articles of association of both the companies.
 - (c) A certified copy of the resolution of the Board of Directors proposing the extension of the financial year.
 - (d) Requisite fee payable to the Central Government under Rules.

(b) Remedy against order of SEBI: ABC Limited was penalized by the SEBI. The following remedies are available to the Company:

- (1) **Appeal to the Securities Appellate Tribunal:** Section 15T of the SEBI Act, 1992 provides that any person aggrieved by an order of the Board may prefer an appeal to the Securities Appellate Tribunal. Such appeal shall be filed within 45 days from the date on which a copy of the order of the Board was received. However, the Tribunal may entertain an appeal after the expiry of the said period if it is satisfied that there was sufficient cause for not filing it within the said period of limitation.
- (2) **Appeal to the Supreme Court:** Section 15Z of the SEBI Act, 1992 provides that any person aggrieved by the decision or order of the SAT may file an appeal to the Supreme Court within 60 days from the date of communication of the decision or order on any question of law arising out of such order. The Supreme Court may entertain such appeal even after the expiry of said period

of limitation if there was reasonable cause for such delay.

- 6 (a) Appointment of Additional Director in a Bank by the RBI:** Under Section 36AA of the Banking Regulation Act, 1949, RBI can terminate any Chairman, Director, Chief Executive, other officials or any employee of the bank where it considers desirable to do so particularly when RBI is of the opinion that conduct of such persons is detrimental to the interest of the depositors or for securing proper management of the banking company. Before such termination concerned person should be given opportunity to be heard of. Such terminated officials can make appeal to the Central Govt. within 30 days from the date of communication of such termination order. The decision of the Central Government cannot be called into question. In case an order is issued pursuant to this section the concerned person shall cease to hold his office for a period of not exceeding 5 years as may be specified in the order. Contravention of the above provision shall be punishable with a fine, which may extend to Rs. 250 per day.

Any such order shall be valid for a period not exceeding three years or such further periods of not exceeding three years at a time as RBI may specify. Under section 36AB: RBI is empowered to appoint additional Directors for the banking company with effect from the date to be specified in the order, in the interest of the bank or that of depositors. Such additional directors shall hold office for a period not exceeding three years or such further periods not exceeding three years at a time.

- (b)** As per section 591 companies falling under the following two classes shall be known as foreign companies namely:

- (i) companies incorporated outside India which, after the commencement of this act, establish a place of business within India, and
- (ii) companies incorporated outside India which have, before the commencement of this act, established a place of business within India and continue to have an established place of business within India at the commencement of this act. (2) notwithstanding anything contained in sub-section (1), where not less than fifty percent of the paid up share capital (whether equity or preference or partly equity and partly preference) of a company incorporated outside Indian and having an established place of business in India, is held by one or more citizens of Indian or by one or more bodies corporate incorporated in India, or by one or more citizens of Indian and one or more bodies corporate incorporated in India, whether singly or in the aggregate, such company shall comply with such of the provisions of this act as may be prescribed with regard to the business carried on by it in India, as if it were a company incorporated in India.

Here as more than 50% of the paid-up capital is held by Indian citizen and Indian company M/s Joel Ltd. shall be treated as Indian company. It shall have to comply with such provision of the act as may be prescribed as if it

were a company incorporated in India.

Joel Ltd. has to submit the following document with the registrar of companies with 30 days of establishment of business in India.

- (a) a certified copy of the charter, statutes, or memorandum and articles, of the company or other instrument constituting or defining the constitution of the company; and, if the instrument is not in the English language, a certified translation thereof.
- (b) the full address of the registered or principal office of the company;
- (c) a list of the directors and secretary of the company, containing the particulars mentioned in sub-section (2).
- (d) the name and address or the names and addresses of the some one or more persons resident in India, authorized to accept on behalf of the company service of process and any notices or other documents required to be served on the company; and
- (e) the full address of the office of the company in India which is deemed to be its principal place of business in India.

- 7 (a) **Penal provisions:** Section 11(3) of the Foreign Exchange Management Act, 1999 states that where any authorized person contravenes any direction given by the Reserve Bank of India under the said Act or fails to file any return as directed by the Reserve Bank of India, the Reserve Bank of India may, after giving reasonable opportunity of being heard impose a penalty which may extend to Rs. 10,000/- and in the case continuing contraventions with an additional penalty which may extend to Rs. 2,000/- for every day during which such contravention continues.

- (b) **Term of office of chairperson and other members are contained in Section 10 of the Competition Act, 2002 :** As per this section the chairperson and every other member shall hold office as such for a term of five years from the date on which he enters upon his office and shall be eligible for re-appointment. They shall not hold office as such after attaining the age of sixty-five years. [Section 10(1)]

A vacancy caused by the resignation or removal of the chairperson or any other member by death or otherwise shall be filled by fresh appointment in accordance with the provisions of Sections 8 and 9 of the Act. [Section 10(2)]

Keeping the above provision in mind Mr. RKP can be appointed as member of the commission for a term of 5 years as he is aged 56 years on 1-1-09. He can also be reappointed but his reappointment will be only up to the age of 65 years. If Mr. RKP resigns as member after working for two years the resulting vacancy can be filled up by fresh appointment approved by the Selection Committee and the Chairman has no power to fill up the vacancy on his own.

- (c) As per Producer Companies (General Reserves) Rules, 2003 issued by the Department of Company Affairs (Presently, Ministry of Corporate Affairs), Ministry of Finance, Government of India on 7th August, 2003 a producer company formed and registered under section 581C of the Companies Act, 1956, shall make investments from and out of its general reserves in the following manner, namely:-
- (a) in approved securities, fixed deposits, units and bonds issued by the Central or State Governments or cooperative societies or scheduled bank; or
 - (b) in a co-operative bank, state co-operative bank, co-operative land development bank or central co-operative bank; or
 - (c) with any other scheduled bank; or
 - (d) in any of the securities specified in section 20 of the Indian Trusts Act, 1882; or
 - (e) in the shares or securities of any other multi-state co-operative society or any co-operative society; or
 - (f) in the shares, securities or assets of a public financial institutions specified under section 4A of the Companies Act, 1956.
- (d) The normal function of a proviso is to except something out of the enactment or to qualify something stated in the enactment which would be within its purview if the proviso were not there. The effect of the proviso is to qualify the preceding enactment which is expressed in terms which are too general. As a general rule, a proviso is added to an enactment to qualify or create an exception to what is in the enactment. Ordinarily a proviso is not interpreted as it stating a general rule.
- It is a cardinal rule of interpretation that a proviso to a particular provision of a statute only embraces the field which is covered by the main provision. It carves out an exception to the provision to which it has been enacted as a proviso and not to the other. (*Ram Narain Sons Ltd. Vs. Assistant Commissioner of Sales Tax*, A.I.R, 1995 Sc 765)
- An explanation is at times appended to a Section to explain the meaning of the text of the section. An explanation may be added to include something within the Section or to exclude something from it. An explanation should normally be so read as to harmonise with and clear up any ambiguity in the main section. It should not be so construed as to widen the ambit of the section.
- (e) **Asset Reconstruction:** 'Asset Reconstruction' means acquisition by any securitization company or reconstruction company of any right or interest of any bank or financial institution in any financial assistance for the purpose of realization of such financial assistance. (Section 2(b) of Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002.

Financial Assets

Financial Assets' means debt or receivables and includes:

a claim to any debt or receivables or part thereof, whether secured or unsecured; or
any debt or receivables secured by mortgage of, or charge on, immovable property;
or a mortgage, charge, hypothecation or pledge of movable property; or

any right or interest in the security, whether full or part underlying such debt or
receivables; or

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)).