

MOCK TEST PAPER 1
INTERMEDIATE (NEW): GROUP – I
PAPER – 2: CORPORATE AND OTHER LAWS
ANSWERS

Division A

1. (i) (c)
(ii) (d)
(iii) (c)
2. (i) (b)
(ii) (a)
3. (d)
4. (a)
5. (b)
6. (d)
7. (b)
8. (d)
9. (a)
10. (a)
11. (c)
12. (c)
13. (a)
14. (c)
15. (a)
16. (a)
17. (b)

Division B

1. (a) **Issue of bonus shares:** As per Section 63 of the Companies Act, 2013, a company may issue fully paid-up bonus shares to its members, in any manner whatsoever, out of—
 - (i) its free reserves;
 - (ii) the securities premium account; or
 - (iii) the capital redemption reserve account:

Provided that no issue of bonus shares shall be made by capitalising reserves created by the revaluation of assets.

As per the given facts, ABC Ltd. has total eligible amount of ₹12 lakhs (i.e. 5.00+3.00+4.00) out of which bonus shares can be issued and the total share capital is ₹ 30.00 lakhs.

Accordingly:

- (i) For issue of 1:3 bonus shares, there will be a requirement of ₹ 10 lakhs (i.e., $\frac{1}{3} \times 30.00$ lakh) which is well within the limit of available amount of ₹ 12 lakhs. So, Silver Oak Limited can go ahead with the bonus issue in the ratio of 1:3.
- (ii) In case Silver Oak Limited intends to issue bonus shares in the ratio of 1:2, there will be a requirement of ₹ 15 lakhs (i.e., $\frac{1}{2} \times 30.00$ lakh). Here in this case, the company cannot go ahead with the issue of bonus shares in the ratio of 1:2, since the requirement of ₹ 15 Lakhs is exceeding the available eligible amount of ₹ 12 lakhs.

- (b) The given problem is based on the proviso provided in the section 127 (d) of the Companies Act, 2013. As per the law where the dividend is declared by a company and there remains calls in arrears and any other sum due from a member, in such case no offence shall be deemed to have been committed where the dividend has been lawfully adjusted by the company against any sum due to it from the shareholder.

As per the facts given in the question, Mr. A is holding equity shares of face value of ₹ 10 Lakhs and has not paid an amount of ₹ 1 lakh towards call money on shares. Referring to the above provision, Mr. A is eligible to get ₹ 1.20 lakh towards dividend, out of which an amount of ₹ 1 lakh can be adjusted towards call money due on his shares. ₹ 20,000 can be paid to him in cash or by cheque or in any electronic mode.

According to the above mentioned provision, company can adjust sum of ₹ 1 lakh due towards call money on shares against the dividend amount payable to Mr. A.

- (c) As per the provisions of Section 141(3)(d) of the Companies Act, 2013, a person who, or his relative or partner is holding any security of or interest in the company or its subsidiary, or of its holding or associate company or a subsidiary of such holding company shall not be appointed as an auditor of the Company.

However, the proviso to the said section states that the above restriction will not apply where such relative holds security or interest in any of the above companies of face value not exceeding ₹ 1,00,000 [as prescribed under the *Company (Audit and Auditors) Rules, 2014*].

In the given instance, CA. Sana is not disqualified to be appointed as a statutory auditor in Hot Ltd. due to the fact that the value of securities held by his brother (relative) is of face value of ₹ 95,000 in the said company, which is within the prescribed limit.

- (d) According to section 133 of the Indian Contract Act, 1872, where there is any variance in the terms of contract between the principal debtor and creditor without surety's consent, it would discharge the surety in respect of all transactions taking place subsequent to such variance.

Accordingly, Y cannot sue X, because a surety (X) is discharged from liability when, without his consent, the creditor makes any change in the terms of his contract with the principal debtor (Z), no matter whether the variation is beneficial to the surety or does not materially affect the position of the surety.

- (e) The promissory note is an unconditional promise in writing. In the above question the amount is certain but the date and name of payee is missing, thus making it a bearer instrument. As per Reserve Bank of India Act, 1934, a promissory note cannot be made payable to bearer - whether on demand or after certain days. Hence, the instrument is illegal as per Reserve Bank of India Act, 1934 and cannot be legally enforced.

2. (a) Section 101 of the Companies Act, 2013 states that to properly call a general meeting notice of at least 21 clear days', before the meeting, should be given to all the members, legal representative of any deceased member or the assignee of insolvent members, the auditors and directors, in writing or electronic mode or other prescribed mode.

Generally, general meetings need to be called by giving at least a notice of 21 clear days.

However, a general meeting may be called after giving shorter notice than that specified in this sub-section if consent, in writing or by electronic mode, is accorded thereto in the case of an annual general meeting, by not less than ninety-five per cent. of the members entitled to vote thereat

In the given question, the Annual General Meeting (AGM) was called by giving less than 21 days clear days notice. Also, consent for calling the meeting at a shorter notice period was given by only 90% members (i.e. less than 95% members). Hence, such meeting can not be said to be validity called.

- (b) (i) The situation as stated in the question relates to the creation of a casual vacancy in the office of an auditor due to resignation of the auditor before the Annual General Meeting in case of a company other government company. Under section 139 (8)(i) of the Companies Act, 2013, any casual vacancy in the office of an auditor arising as a result of his resignation, such vacancy can be filled by the Board of Directors within 30 days thereof and in addition the appointment of the new auditor shall also be approved by the company at a general meeting convened within 3 months of the recommendation of the Board and he shall hold the office till the conclusion of the next annual general meeting.
- (ii) **Persons responsible to maintain books:** As per Section 128 (6) of the Companies Act, 2013, the person responsible to take all reasonable steps to secure compliance by the company with the requirement of maintenance of books of account etc. shall be:
- (a) Managing Director,
 - (b) Whole-Time Director, in charge of finance
 - (c) Chief Financial Officer
 - (d) Any other person of a company charged by the Board with duty of complying with provisions of section 128.
- (c) **Co-sureties liable to contribute equally** (Section 146 of the Indian Contract act, 1872): Equality of burden is the basis of Co-suretyship. This is contained in section 146 which states that “when two or more persons are co-sureties for the same debt, or duty, either jointly, or severally and whether under the same or different contracts and whether with or without the knowledge of each other, the co-sureties in the absence of any contract to the contrary, are liable, as between themselves, to pay each an equal share of the whole debt, or of that part of it which remains unpaid by the principal debtor”.

Accordingly, on the default of D in payment, B cannot escape from his liability. All the three sureties A, B and N are liable to pay equally, in absence of any contract between them.

(d) Essential Characteristics of Negotiable Instruments

1. It is necessarily in writing.
2. It should be signed.
3. It is freely transferable from one person to another.
4. Holder’s title is free from defects.
5. It can be transferred any number of times till its satisfaction.
6. Every negotiable instrument must contain an unconditional promise or order to pay money. The promise or order to pay must consist of money only.
7. The sum payable, the time of payment, the payee, must be certain.
8. The instrument should be delivered. Mere drawing of instrument does not create liability.

3. (a) (1) **Meaning of Abridged Prospectus:** - According to Section 2(1) of the Companies Act, 2018, an abridged prospectus means a memorandum containing such salient features of a prospectus as may be specified by the Securities and Exchange Board by making regulations in this behalf.

(2) **Circumstances under which the abridged prospectus need not accompany the application forms:** Section 33 (1) of the Companies Act, 2013 states that no application form for the purchase of any of the securities of a company can be issued unless such form is accompanied by an abridged prospectus.

In terms of the Proviso to section 33 (1) an abridged prospectus need not accompany the application form if it is shown that the form of application was issued:

(i) In connection with a bona fide invitation to a person to enter into an underwriting agreement with respect to such securities; or

(ii) Where the securities are not offered to the public.

(b) According to Section 139(2) of the Companies Act, 2013, no listed company or a company belonging to such class or classes of companies as may be prescribed, shall appoint or re-appoint—

(a) an individual as auditor for more than one term of five consecutive years; and

(b) an audit firm as auditor for more than two terms of five consecutive years.

Provided that –

(i) an individual auditor who has completed his term under clause (a) shall not be eligible for re-appointment as auditor in the same company for five years from the completion of his term;

(ii) an audit firm which has completed its term under clause (b), shall not be eligible for re-appointment as auditor in the same company for five years from the completion of such term.

Provided further that as on the date of appointment no audit firm having a common partner or partners to the other audit firm, whose tenure has expired in a company immediately preceding the financial year, shall be appointed as auditor of the same company for a period of five years.

Under Rule 6(3)(ii)(b) of The Companies (Audit and Auditors) Rules, 2014. if a partner, who is in charge of an audit firm and also certifies the financial statements of the company, retires from the said firm and joins another firm of chartered accountants, such other firm shall also be ineligible to be appointed for a period of five years.

Here Mr. Yash has retired from PQR Firm and joined Gupta & Gupta Firm. Mr. Yash was a partner in PQR firm, where he certifies the financial statement of the company, and retires from the said firm and joins Gupta & Gupta firm. Hence Gupta & Gupta Firm will also be ineligible, to be appointed as auditor firm for a period of 5 years.

(c) **Person to be called as a holder:** As per section 8 of the Negotiable Instruments Act, 1881, 'holder' of a Negotiable Instrument means any person entitled in his own name to the possession of it and to receive or recover the amount due thereon from the parties thereto.

On applying the above provision in the given cases-

(1) 'M' is not a 'holder' because to be called as a 'holder' he must be entitled not only to the possession of the instrument but also to receive the amount mentioned therein.

(2) No, 'M' is not a holder. While the agent may receive payment of the amount mentioned in the cheque, yet he cannot be called the holder thereof because he has no right to sue on the instrument in his own name.

(d) **Dictionary Definitions:** First we refer the Act in question to find out if any particular word or expression is defined in it. Where we find that a word is not defined in the Act itself, we may refer

to dictionaries to find out the general sense in which that word is commonly understood. However, in selecting one out of the several meanings of a word, we must always take into consideration the context in which it is used in the Act. It is the fundamental rule that the meanings of words and expressions used in an Act must take their colour from the context in which they appear. Further, judicial decisions laying down the meaning of words in construing statutes in *pari materia* will have greater weight than the meaning furnished by dictionaries. However, for technical terms, reference may be made to technical dictionaries.

4. (a) Doctrine of Indoor Management

According to this doctrine, persons dealing with the company need not inquire whether internal proceedings relating to the contract are followed correctly, once they are satisfied that the transaction is in accordance with the memorandum and articles of association.

Stakeholders need not enquire whether the necessary meeting was convened and held properly or whether necessary resolution was passed properly. They are entitled to take it for granted that the company had gone through all these proceedings in a regular manner.

The doctrine helps to protect external members from the company and states that the people are entitled to presume that internal proceedings are as per documents submitted with the Registrar of Companies.

The doctrine of indoor management is opposite to the doctrine of constructive notice. Whereas the doctrine of constructive notice protects a company against outsiders, the doctrine of indoor management protects outsiders against the actions of a company. This doctrine also is a safeguard against the possibility of abusing the doctrine of constructive notice.

(b) Rule 2 (1) (c) of the *Companies (Acceptance of Deposit) Rules, 2014* states various amounts received by a company which will not be considered as deposits. In terms of this Rule the answers to the given situations shall be as under:

(i) ₹ 5,00,000 raised by Rohit Limited through issue of non-convertible debentures not constituting a charge on the assets of the company and listed on recognised stock exchange as per the applicable regulations made by the SEBI, will not be considered as deposit in terms of sub-clause (ixa) of Rule 2 (1) (c).

(ii) ₹ 2,00,000 received by Rishi Limited from its employee Mr. Tarun, who draws an annual salary of ₹ 1,50,000, as a non-interest bearing security deposit under a contract of employment will be considered as deposit in terms of sub-clause (x) of Rule 2 (1) (c), for the amount received is more than his annual salary of ₹ 1,50,000.

(c) According to section 5 of the General Clauses Act, 1897, where any Central Act has not specifically mentioned a particular date to come into force, it shall be implemented on the day on which it receives the assent of the Governor General in case of a Central Acts made before the commencement of the Indian Constitution and/or, of the President in case of an Act of Parliament.

Hence, in the given question, SEBI (Issue of Capital and Disclosure Requirements) (Fifth Amendment) Regulations, 2015 shall come into enforcement on 1st January, 2016 rather than the date of its notification in the gazette.

(d) **Grammatical Interpretation and its exceptions:** 'Grammatical interpretation' concerns itself exclusively with the verbal expression of the law, it does not go beyond the letter of the law. In all ordinary cases, 'grammatical interpretation' is the sole form allowable. The Court cannot take from or add to modify the letter of the law.

This rule, however, is subject to some exceptions:

(i) Where the letter of the law is logically defective on account of ambiguity, inconsistency or incompleteness. As regard the defect to ambiguity, the Court is under a duty to travel beyond the letter of the law so as to determine from the other sources the true intention of the

legislature. In the case of the statutory expression being defective on account of inconsistency, the court must ascertain the spirit of the law.

- (ii) If the text leads to a result which is so unreasonable that it is self-evident that the legislature could not mean what it says, the court may resolve such impasse by inferring logically the intention of the legislature.

5. (a) **Small Company:** According to Section 2(85) of the Companies Act, 2013, Small Company means a company, other than a public company,—

- (i) paid-up share capital of which does not exceed fifty lakh rupees or such higher amount as may be prescribed which shall not be more than ten crore rupees; and
- (ii) turnover of which as per its last profit and loss account does not exceed two crore rupees or such higher amount as may be prescribed which shall not be more than one hundred crore rupees.

Nothing in this clause shall apply to—

- (A) a holding company or a subsidiary company;
- (B) a company registered under section 8; or
- (C) a company or body corporate governed by any special Act.

As per the Companies (Specification of Definitions Details) Rules, 2014, for the purposes of sub-clause (i) and sub-clause (ii) of clause (85) of section 2 of the Act, paid up capital and turnover of the small company shall not exceed rupees two crores and rupees twenty crores respectively.

- (1) In the present case, New Private Ltd., a company registered under the Companies Act, 2013 with a paid up share capital of ₹ 70 lakh and having turnover of ₹ 30 crore. Since, only one criteria of share capital not exceeding ₹ 2 crores is met, but the second criteria of turnover not exceeding ₹ 20 crores is not met and the provisions require both the criteria to be met in order to avail the status of a small company, New Private Ltd. cannot avail the status of small company.
- (2) If the turnover of the company is ₹ 15 crore, then both the criteria will be fulfilled and New Private Ltd. can avail the status of small company.

(b) In this respect following provisions are required to be observed as mentioned in Rule 7 of the *Companies (Acceptance of Deposits) Rules, 2014*:

No person including a company that is in the business of providing trusteeship services shall be appointed as a trustee for the depositors, if the proposed trustee:

- (a) is a director, key managerial personnel or any other officer or an employee of the company or of its holding, subsidiary or associate company or a depositor in the company;
- (b) is indebted to the company, or its subsidiary or its holding or associate company or a subsidiary of such holding company;
- (c) has any material pecuniary relationship with the company;
- (d) has entered into any guarantee arrangement in respect of principal debts secured by the deposits or interest thereon;
- (e) is related to any person specified in clause (a) above.

(c) **On the basis of reward, bailment can be classified into two types:**

- (i) **Gratuitous Bailment:** The word gratuitous means free of charge. So, a gratuitous bailment is one when the provider of service does it gratuitously i.e. free of charge. Such bailment would be either for the exclusive benefits of bailor or bailee.

- (ii) **Non-Gratuitous Bailment:** Non gratuitous bailment means where both the parties get some benefit i.e. bailment for the benefit of both bailor & bailee
- (d) **“Duty to be taken pro rata in enactments”:** According to section 12 of the General Clauses Act, 1897, where, by any enactment now in force or hereafter to be in force, any duty of customs or excise or in the nature thereof, is leviable on any given quantity, by weight, measure or value of any goods or merchandise, then a like duty is leviable according to the same rate on any greater or less quantity.

Pro rata is a Latin term used to describe a proportionate allocation.

Example: Where several debtors are liable for the whole debt and each is liable for his own share or proportion only, they are said to be bound pro rata.