MOCK TEST PAPER 1

INTERMEDIATE : GROUP – I

PAPER – 2: CORPORATE AND OTHER LAWS

ANSWERS

Division A

I. 1. (b)

2. (c)

3. (b)

II. 4. (a)

5. (a)

6. (c)

7. (b)

8. (d)

9. (c)

10. (b)

11. (c)

12. (c)

13. (b)

14. (b)

15. (c)

16. (a)

17. (c)

18. (a)

19. (a)

20. (b)

21. (b)

22. (d)

Division B

1. (a) This given problem is based on sub-clause (87) of Clause 2 read with section 19 of the Companies Act, 2013.

As per sub-clause (87) of Clause 2 of the Companies Act, 2013 "subsidiary company" or "subsidiary", in relation to any other company (i.e., the holding company), means a company in which the holding company—

(i) controls the composition of the Board of Directors; or

(ii) exercises or controls more than one-half of the total voting power either at its own or together with one or more of its subsidiary companies.

For the purposes of this clause, Explanation is given providing that a company shall be deemed to be a subsidiary company of the holding company even if the control referred to in point (i) or

point (ii) above, is of another subsidiary company of the holding company.

Whereas section 19 provides that, no company shall, hold any shares in its holding company and no holding company shall allot or transfer its shares to any of its subsidiary companies and any such allotment or transfer of shares of a company to its subsidiary company shall be void.

Provided that nothing in this sub-section shall apply to a case where the subsidiary company is a shareholder even before it became a subsidiary company of the holding company.

Here in the instant case, Kapila Limited issued 10,000 equity shares on 1.4.2021 whereby Kusha Limited & Prem Limited holds 4000 & 2000 shares respectively in Kapila Ltd., Considering 1 share = 1 vote, Kusha Limited and Prem Limited together holds more than one-half (50%) of the total voting power. Therefore, Kapila Limited will be subsidiary to Kusha Limited & Prem Limited from 1.4.2021.

Whereas Kapila Limited is already holding 20% equity shares of Red Limited before the date of issue of equity shares i.e. 1.4.2021.

Further, Red Limited controls the composition of Board of Directors of Kusha Limited and Prem Limited from 01.08.2021. In the light of sub-clause (87) of Clause 2, Red Limited is a holding company of Kusha Limited and Prem Limited (Subsidiary companies).

Following are the answers to the questions:

(i) Yes, Kapila Limited is a subsidiary of Red Limited. In this case Kapila Limited shall be deemed to be a subsidiary company of the holding company (Red Limited) as Red Limited controls the composition of subsidiary companies Kusha Limited & Prem Limited as per explanation to sub-clause (87) of Clause 2.

(ii) Yes, Kapila Limited can hold shares of Red Limited. In this case Kapila Limited is a subsidiary of Red Limited as Kapila Limited was holding 20% of equity shares of Red Limited even before it became a subsidiary company of the Red Limited (i.e. on 01.08.2021), according to the exception to section 19.

(b) (i) As per section 141 (3)(d)(i) an auditor is disqualified to be appointed as an auditor if he, or his relative or partner 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.

In this case Mr. Shepra, a practicing Chartered Accountant holding shares in X Limited cannot be appointed as auditor of X Limited.

(ii) Section 141(3) of the Companies Act, 2013 read with Rule 10 of the Companies (Audit and Auditors) Rules, 2014 provides that a person or a firm who, whether directly or indirectly, has business relationship with the company, or its subsidiary, or its holding or associate company or subsidiary of such holding company or associate company, shall not be eligible for appointment as an auditor of a company.

The term business relationship shall be construed as any transaction entered into for a commercial purpose except –

- commercial transactions which are in the nature of professional services permitted to be rendered by an auditor or audit firm under the Act and the Chartered Accountant Act, 1949 and the rules or the regulations made under those Act;

- commercial transactions which are in the ordinary course of business of the company at arm's length price – like sale of products or services to the auditors, as customer, in the ordinary course of business, by companies engaged in the business of telecommunications, airlines, hospitals, hotels and such other similar businesses.

In the given question, since the transaction is at arm's length price so Mr. Showik can be appointed as an auditor of Primus Hotels Limited.

(c) According to section 157 of the Contract Act, 1872, if the bailee, without the consent of the bailor, mixes the goods of the bailor with his own goods, in such a manner that it is impossible to separate the goods bailed from the other goods and deliver them back, the bailor is entitled to be compensated by the bailee for the loss of the goods.

In the given question, Saksham's employee mixed high quality sugar bailed by Anay and then packaged it for sale. The sugars when mixed cannot be separated. As Saksham's employee has mixed the two kinds of sugar, he (Saksham) must compensate Anay for the loss of his sugar.

(d) **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—

(i) In the given question, though Madan is in possession of the cheque but is not entitled to the possession of it in his own name (he got the cheque on the floor of metro coach). Hence, Madan is not a holder of the Instrument.

(ii) In the given question though the agent (i.e. Preeti) may receive payment of the amount mentioned in the cheque, yet she cannot be called the holder thereof because she has no right to sue on the instrument in her own name. Hence, Preeti is not a holder.

2. **(a)** **(i)** According to section 96 of the Companies Act, 2013, first annual general meeting of the company should be held within nine months from the closing of the first financial year.

Hence, the statement that the first Annual General Meeting (AGM) of a company shall be held within a period of six months from the date of closing of the first financial year is **incorrect**.

(ii) According to proviso to section 96(1), the Registrar may, for any special reason, extend the time within which any annual general meeting, other than the first annual general meeting, shall be held, by a period not exceeding three months.

Thus, the Registrar cannot extend (for any reason) the time period within which the first AGM shall be held. Given statement is **incorrect.**

(b) According to the provisions of section 138 of the Companies Act, 2013, read with Rule 13 of the Companies (Accounts) Rules, 2014, the following class of companies shall be required to appoint an internal auditor which may be either an individual or a partnership firm or a body corporate, namely:

(1) every listed company;

(2) every unlisted public company having-

(A) paid up share capital of 50 crore rupees or more during the preceding financial year; or

(B) turnover of 200 crore rupees or more during the preceding financial year;

(C) outstanding loans or borrowings from banks or financial institutions exceeding one hundred crore rupees or more at any point of time during the preceding financial year; or

(D) outstanding deposits of twenty five crore rupees or more at any point of time during the preceding financial year.

Besides, some private companies are also required to appoint an internal auditor which may be either an individual or a partnership firm or a body corporate.

Thus, Aura limited (which is a listed company) is required to appoint an internal auditor, irrespective of its paid-up share capital or turnover (as the limit of paid- up share capital or turnover is applicable for unlisted public company).

Hence, the advice of the Company Secretary is not correct.

(c) According to section 191 of the Indian Contract Act, 1872, a "Sub-agent" is a person employed by, and acting under the control of, the original agent in the business of the agency.

Section 210 provides that, the termination of the authority of an agent causes the termination (subject to the rules regarding the termination of an agent's authority) of the authority of all sub-agents appointed by him.

In the given question, Ganesh is the agent of Shiva, and Gauri is the agent of Ganesh. Hence, Gauri becomes a sub- agent.

Thus, when Shiva revokes the authority of Ganesh (agent), it results in termination of authority of sub-agent appointed by Ganesh i.e. Gauri (sub-agent).

(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) (i) Meaning of 'Private Placement': As per Explanation I to section 42(3), the term "private placement" means any offer or invitation to subscribe or issue of securities to a select group of persons by a company (other than by way of public offer) through private placement offer-cum-application, which satisfies the conditions specified in section 42.

(ii) 'Time Limit for Allotment of Securities' and 'repayment of application money in case of default in allotment': A company making an offer or invitation under section 42 shall allot its securities within sixty days from the date of receipt of the application money for such securities and if the company is not able to allot the securities within that period, it shall repay the application money to the subscribers within fifteen days from the expiry of sixty days and if the company fails to repay the application money within the aforesaid period, it shall be liable to repay that money with interest at the rate of twelve per cent per annum from the expiry of the sixtieth day.

(b) As per section 139(6) of the Companies Act, 2013, the first auditor of a company, other than a Government company, shall be appointed by the Board of Directors within thirty days from the date of registration of the company and such auditor shall hold office till the conclusion of the first annual general meeting.

Whereas Section 139(1) of the Companies Act, 2013 states that every company shall, at the first annual general meeting (AGM), appoint an individual or a firm as an auditor of the company who shall hold office from the conclusion of 1st AGM till the conclusion of its 6th AGM and thereafter till the conclusion of every sixth AGM.

As per section 139(2), no listed company or a company belonging to such class or classes of companies as may be prescribed, shall appoint or re-appoint an individual as auditor for more than one term of five consecutive years.

As per the given provisions following are the answers:

(i) Appointment of Mr. Guru (as first auditor) by the Board of Directors is valid as per the provisions of section 139(6).

(ii) Appointment of Mr. Guru at the first Annual General Meeting is valid due to the fact that the appointment of the first auditor made by the Board of Directors is a separate appointment and the period of such appointment is not to be considered, while Mr. Guru is appointed in the first Annual General Meeting, which is for the period from the conclusion of the first Annual General Meeting to the conclusion of the sixth Annual General Meeting.

(c) According to section 134 of the Negotiable Instruments Act, 1881, in the absence of a contract to the country, the liability of the maker or drawer of a foreign promissory note or bill of exchange or cheque is regulated in all essential matters by the law of the place where he made the instrument, and the respective liabilities of the acceptor and indorser by the law of the place where the instrument is made payable.

In the given case, since action on the bill is brought against B in India, he is liable to pay interest at the rate of 6% only.

(d) **(i)** **Proviso:** 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 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.

(ii) **Explanation:** 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.

The meaning to be given to an explanation will really depend upon its terms and not on any theory of its purpose.

4. **(a)** **(i)** According to proviso to section 68(2) of the Companies Act, 2013, no offer of buy-back, shall be made within a period of one year from the date of the closure of the preceding offer of buy-back, if any.

Section 68 (8) casts an obligation that where a company completes a buy-back of its shares or other specified securities under this section, it shall not make further issue of same kind of shares including allotment of further shares under section 62 (1) (a) or other specified securities within a period of six months except by way of bonus issue or in the discharge of subsisting obligations such as conversion of warrants, stock option schemes, sweat equity or conversion of preference shares or debentures into equity shares.

Keeping in view of the above provisions, the statement "the offer of buy-back of its own shares by a company shall not be made within a period of six months from the date of the closure of the preceding offer of buy back, if any and cooling period to make further issue of same kind of shares including allotment of further shares shall be a period of one year from the completion of buy back subject to certain exceptions" is not valid.

(ii) Information Memorandum together with Shelf Prospectus is deemed Prospectus. The expression "shelf prospectus" means a prospectus in respect of which the securities or class of securities included therein are issued for subscription in one or more issues over a certain period without the issue of a further prospectus. [Explanation to Section 31]

Any class or classes of companies, as the Securities and Exchange Board may provide by regulations in this behalf, may file a shelf prospectus with the Registrar at the stage-

(i) of the first offer of securities included therein which shall indicate a period not exceeding one year as the period of validity of such prospectus which shall commence from the date of opening of the first offer of securities under that prospectus, and

(ii) in respect of a second or subsequent offer of such securities issued during the period of validity of that prospectus,

No further prospectus is required for issue of securities. [Sub-section (1)]

Hence, the proposal of ABC Limited to take into account the concept of deemed prospectus is correct.

(b) According to Rule 2 (1) (c) of the Companies (Acceptance of Deposits) Rules, 2014, the following amount is not considered as deposit:

Any amount brought in by the promoters of the company by way of unsecured loan in pursuance of the stipulation of any lending financial institution or a bank subject to the fulfillment of following conditions:

(a) the loan is brought because of the stipulation imposed by the lending institutions on the promoters to contribute such finance;

(b) the loan is provided by the promoters themselves or by their relatives or by both; and

(c) such exemption shall be available only till the loans of financial institution or bank are repaid and not thereafter.

Hence, in the instant case, the unsecured loan contributed by promoters of Green Limited will not be regarded as deposit as the unsecured loan is brought because of the stipulation imposed by the SIDCL and the loan is provided by the promoters themselves.

(c) (i) 'Things attached to the earth' have been held to be immovable property: This statement is valid.

As per section 3(26) of the General Clauses Act, 1897, 'Immovable Property' shall include:

(1) Land,

(2) Benefits to arise out of land, and

(3) Things attached to the earth, or

(4) Permanently fastened to anything attached to the earth.

It is an inclusive definition. The four elements to the definition includes 'things permanently fastened to anything attached to the earth'. Hence, the given statement is correct.

(ii) The word 'bullocks' could be interpreted to include 'cows': This statement is not valid.

Where a word connoting a common gender is available but the word used conveys a specific gender, there is a presumption that the provisions of General Clauses Act, 1897 do not apply. Thus, the word 'bullocks' could not be interpreted to include 'cows'.

(d) **Associated Words to be Understood in Common Sense Manner**: When two words or expressions are coupled together one of which generally excludes the other, obviously the more general term is used in a meaning excluding the specific one. On the other hand, there is the concept of *'Noscitur A Sociis'* ('it is known by its associates'), that is to say 'the meaning of a word is to be judged by the company it keeps'. When two or more words which are capable of analogous (similar or parallel) meaning are coupled together, they are to be understood in their cognate sense (i.e. akin in origin, nature or quality). They take, as it were, their colour from each other, i.e., the more general is restricted to a sense analogous to the less general. It is a rule wider than the rule of *ejusdem generis*, rather *ejusdem generis* is only an application of the *noscitur a sociis*. It must be borne in mind that *nocitur a sociis*, is merely a rule of construction and it cannot prevail in cases where it is clear that the wider words have been deliberately used in order to make the scope of the defined word correspondingly wider.

5. **(a)** **(i)** According to section 8(6) of the Companies Act, 2013, the Central Government may by order revoke the licence of the company where the company contravenes any of the requirements or the conditions of section 8 subject to which a licence is issued or where the affairs of the company are conducted fraudulently, or in violation of the objects of the company or prejudicial to public interest, and on revocation, the Registrar shall put 'Limited' or 'Private Limited' against the company's name in the register. But before such revocation, the Central Government must give it a written notice of its intention to revoke the licence and opportunity to be heard in the matter.

Hence, in the instant case, the Central Government can revoke the license given to Gully Gilli Danda Club as section 8 company, as the affairs of the company are conducted fraudulently and dividend was paid to its members which is in contravention to the conditions given under section 8.

(ii) Where a licence is revoked, the Central Government may, by order, if it is satisfied that it is essential in the public interest, direct that the company be wound up under this Act or amalgamated with another company registered under this section.

However, no such order shall be made unless the company is given a reasonable opportunity of being heard. [Section 8(7)].

Hence, the stated company may be wound up.

(iii) A company registered under this section shall amalgamate only with another company registered under this section and having similar objects. [Section 8(10)]

In the instant case, Gully Gilli Danda Club cannot be merged with Stick Private Limited as the objects of both the companies are different and not similar.

(b) Section 118 of the Companies Act, 2013 provides that every company shall prepare, sign and keep minutes of proceedings of every general meeting, including the meeting called by the requisitionists and all proceedings of meeting of any class of shareholders or creditors or Board of Directors or committee of the Board and also resolution passed by postal ballot within thirty days of the conclusion of every such meeting concerned. Minutes kept shall be evidence of the proceedings recorded in a meeting.

By virtue of Rule 25 of the Companies (Management and Administration) Rules, 2014 read with section 118 of the Companies Act, 2013, each page of every such book shall be initialled or signed and the last page of the record of proceedings of each meeting or each report in such books shall be dated and signed by, in the case of minutes of proceedings of a general meeting, by the chairman of the same meeting within the aforesaid period of thirty days or in the event of the death or inability of that chairman within that period, by a director duly authorized by the Board for the purpose.

Therefore, the minutes of the meeting referred to in the case of A Ltd. can be signed in the absence of Mr. B, by any director, authorized by the Board in this respect.

(c) (i) **Contract of guarantee:** As per the provisions of section 126 of the Indian Contract Act, 1872, a contract of guarantee is a contract to perform the promise made or discharge the liability, of a third person in case of his default.

(ii) Three parties are involved in a contract of guarantee:

Surety- person who gives the guarantee,

Principal debtor- person in respect of whose default the guarantee is given,

Creditor- person to whom the guarantee is given

(d) Good Faith

In general, anything done with due care and attention, which is not malafide is presumed to have been done in good faith.

But, according to section 3(22) of the General Clauses Act, 1897, a thing shall be deemed to be done in "good faith" where it is in fact done honestly, whether it is done negligently or not.

The question of good faith under the General Clauses Act is one of fact. It is to determine with reference to the circumstances of each case.

It is therefore understood that the General Clauses Act, 1897 considers the honesty in doing the Act as a primary test to constitute the thing done in good faith and therefore the act done honestly but with negligence may also be termed as done in good faith as per the General Clauses Act, 1897.