

PAPER – 2 : CORPORATE & OTHER LAW

Question No. 1 is compulsory.

Attempt any **three** questions from the remaining **four** questions.

Question 1

- (a) (i) Chhavish, an Indian citizen and resident of India formed “Ekta Readymade Garments (OPC) Private Ltd.” as One Person Company on 1st April 2018 with his wife Mrs. Jyoti as nominee. The authorized and paid-up share capital of the company is ₹ 35 lakhs. He got in touch with a readymade garments buyer and was expecting to receive a substantial order by August 2020 where final delivery will be completed by December 2020. To expand the production capacity, the decided to invest an additional capital of ₹ 10 lakhs in plant and machinery. As a result, the company’s authorized and paid-up share capital is now ₹ 45 Lakhs. Promoter of the company seeks your advice. Considering the case and referring the provisions of the Companies Act, 2013, advice:
- (A) Who is eligible to act as a member of OPC?
- (B) Whether “Ekta Readymade Garments (OPC) Private Ltd.” can convert into any other kind of company as on 1st December 2020?
- (C) If the company increases its paid up share capital by ₹ 30 lakhs in August, 2019, can it be converted in any other kind of company immediately?

(3 Marks)

- (ii) Following is the extract of the Balance sheet Beltex Ltd. as on 31st March, 2020:

Particulars		Amount (₹)
Equity & Liabilities		
(1) Shareholder’s Fund		
(a) Share Capital:		
Authorized Capital:		
10,000, 12% Preference Shares of ₹ 10 each	1,00,000	
1,00,000 equity shares of ₹ 10 each	10,00,000	<u>11,00,000</u>
Issued & Subscribed Capital:		
8000, 12% Preference Shares of ₹ 10 each fully paid up		80,000
90,000 equity shares of ₹ 10 each, ₹ 8 paid up		7,20,000

(b) Reserve and Surplus		
General Reserve	1,20,000	
Capital Reserve	75,000	
Securities Premium	25,000	
Surplus in statement of P&L	<u>2,00,000</u>	<u>4,20,000</u>
(2) Non-Current Liabilities:		
(a) Long-term borrowings:		
Secured Loan: 12% partly convertible		
Debenture @ ₹100 each		5,00,000

On 1st April, 2020 the company has made final call at ₹ 2 each on 90,000 Equity Shares. The call money was received by 25th April, 2020. Thereafter, the company decided to capitalize its reserves by way of bonus @ 1 share for every 4 shares to existing shareholders.

Answer the following questions according to the Companies Act, 2013, in above case:

- (A) Which of the above-mentioned sources can be used by company to issue bonus shares?
- (B) Calculate the amount to be capitalized from free reserves to issue bonus shares?
- (C) If the company did not ask for the final call on April 1st, 2020. Can it still issue bonus shares to its members? **(3 Marks)**
- (b) (i) Mr. Raman, a Chartered Accountant, was appointed as an auditor of Surya Distributors Ltd., in the AGM of the company held in August, 2020, in which he accepted the assignment. Later on, in November, 2020, he joined as a partner in the Consultancy firm where Mr. Som is also a partner. Mr. Som is also working as a Finance executive of Surya Distributors Ltd. Explaining the provisions of the Companies Act, 2013, decide whether Mr. Raman is required to vacate the office as an auditor. **(2 Marks)**
- (ii) Managing Director of ABC Ltd. himself appointed Mr. Aakash, a practicing chartered accountant as first auditor of the company. Is it a valid appointment? Also explain the provisions of the Companies Act, 2013, in this regard? **(2 Marks)**
- (iii) The Board of Directors of ABC Limited at its board meeting declared dividend on its paid-up equity share capital which was later on approved by the company's Annual General Meeting. In the meantime, the directors diverted the amount of total dividend to be paid to shareholders for purchase of investments for the company. Due to this dividend was paid to shareholders after 45 days declaration.

Examining the provisions of the Companies Act, 2013, state whether the act of directors is in violation of the provisions of the Companies Act, 2013. Also explain what are the consequences of the above act of directors. (2 Marks)

- (c) *Due to urgent need of money amounting to ₹ 3,00,000, Pawan approached Raman and asked him for the money. Raman lent the money on the guarantee of Suraj, Tarun and Usha. Pawan makes default in payment and Suraj pays full amount to Raman. Suraj, afterwards, claimed contribution from Tarun and Usha refused to contribute on the basis that there is no contract between Suraj and him. Examine referring to the provisions of the Indian Contract Act, 1872, whether Tarun can escape from his liability. (4 Marks)*

- (d) *'M' is the holder of a bill of exchange made payable to the order of 'F'.*

The bill of exchange contains the following endorsements in blank:

First endorsement 'N'

Second endorsement 'O'

Third endorsement 'P' and

Fourth endorsement 'Q'

'M' strikes out, without Q's consent, the endorsements by 'O' and 'P'. Decide, with reasons, whether 'M' is entitled to recover anything from 'Q' under the provisions of the Negotiable Instruments Act, 1881. (3 Marks)

Answer

- (a) (i) (A) The memorandum of OPC shall indicate the name of the other person (nominee), who shall, in the event of the subscriber's death or his incapacity to contract, become the member of the company.

Only a natural person who is an Indian citizen whether resident in India or otherwise-

- (a) shall be eligible to incorporate One Person Company (OPC);
- (b) shall be a nominee for the sole member of One Person Company (OPC).

- (B) OPC cannot convert voluntarily into any kind of company unless two years have expired from the date of incorporation, except where the paid up share capital is increased beyond fifty lakh rupees or its average annual turnover during the relevant period exceeds two crore rupees.¹

Ekta Readymade Garments Ltd. was incorporated on 1st April, 2018.

¹ The Ministry of Corporate Affairs w.e.f 1st April, 2021 has removed the condition whereby OPC cannot convert voluntarily into any kind of company unless two years have expired from the date of incorporation, except where the paid up share capital is increased beyond fifty lakh rupees or its average annual turnover during the relevant period exceeds two crore rupees.

Ekta Readymade Garments Ltd. cannot voluntarily convert the OPC into any other kind of company before expiry of two years from 1st April, 2018 i.e. upto 31st March, 2020. Thus, it can convert into any other kind of company as on 1st December, 2020.

- (C) If the paid up share capital of Ekta Readymade Garments Ltd. is increased to ₹ 65 lakhs (35+30), it will be converted into other forms company immediately.

(ii) Issue of Bonus Shares

- (1) According to section 63 (1) 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.

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

- (2) Section 63 (2) provides that the company can issue bonus shares only when the partly paid-up shares, if any outstanding on the date of allotment, are made fully paid-up.

- (A) The following sources can be used by the company to issue bonus shares:

1. General Reserve
2. Securities Premium
3. Surplus in statement of P&L

- (B) Amount of bonus shares to be issued = 90,000 shares x 1/4
= 22,500 shares

Amount that ought to be capitalized for issue of bonus shares = 22,500 x ₹ 10 per share
= ₹ 2,25,000

Total amount available to be capitalized from free reserves to issue bonus shares = 1,20,000+25,000+2,00,000
= ₹ 3,45,000

Hence, the amount to be capitalized from free reserves to issue bonus shares will be ₹ 2,25,000.

- (C) A company can issue bonus shares on only fully paid shares. Hence, if the company did not ask for the final call on 1st April, 2020, it cannot issue bonus shares to its members.

- (b) (i) Section 141(3)(c) of the Companies Act, 2013, prescribes that any person who is a partner or in employment of an officer or employee of the company will be disqualified to act as an auditor of a company. Sub-section (4) of section 141

provides that an auditor who becomes subject, after his appointment, to any of the disqualifications specified in sub-sections (3) of section 141, he shall be deemed to have vacated his office as an auditor.

In the present case, Mr. Raman, an auditor of Surya Distributors Ltd., joined as partner with consultancy firm where Mr. Som is also a partner and Mr. Som is also the Finance executive of Surya Distributors Ltd. Hence, Mr. Raman has attracted clause (3)(c) of section 141 and, therefore, he shall be deemed to have vacated office of the auditor of Surya Distributors Ltd.

- (ii) Section 139(6) of the Companies Act, 2013 provides that “the first auditor or auditors of a company shall be appointed by the Board of directors within 30 days from the date of registration of the company”.

In the instant case, the appointment of Mr. Aakash, a practicing Chartered Accountant as first auditor by the Managing Director of ABC Ltd. by himself is in violation of section 139(6) of the Companies Act, 2013, which requires the Board of Directors to appoint the first auditor of the company.

In view of the above, the Managing Director of ABC Ltd. cannot appoint the first auditor of the company himself.

- (iii) According to section 124 of the Companies Act, 2013, where a dividend has been declared by a company but has not been paid or claimed within 30 days from the date of the declaration, the company shall, within 7 days from the date of expiry of the said period of 30 days, transfer the total amount of dividend which remains unpaid or unclaimed to a special account to be opened by the company in any scheduled bank to be called the Unpaid Dividend Account.

Further, according to section 127 of the Companies Act, 2013, where a dividend has been declared by a company but has not been paid or the warrant in respect thereof has not been posted within 30 days from the date of declaration to any entitled shareholder, every director of the company shall, if he is knowingly a party to the default, be liable for punishment.

The Board of Directors of ABC Limited at its meeting recommended a dividend on its paid-up equity share capital which was later on approved by the shareholders at the Annual General Meeting. In the meantime, the directors diverted the total dividend to be paid to the shareholders for purchase of investments in the name of the company. As a result, dividend was paid to shareholders after 45 days.

1. Since, declared dividend has not been paid within 30 days from the date of the declaration to any shareholder entitled to the payment of dividend, the company shall, within 7 days from the date of expiry of the said period of 30 days, transfer the total amount of dividend which remains unpaid or unclaimed to the Unpaid Dividend Account.

2. The Board of Directors of ABC Limited has violated section 127 of the Companies Act, 2013 as it failed to pay dividend to shareholders within 30 days due to its decision to divert the total dividend to be paid to shareholders for purchase of investments in the name of the company.

Consequences: The following are the consequences for violation of the above provisions:

- (a) Every director of the company shall, if he is knowingly a party to the default, be punishable with maximum imprisonment of two years and shall also be liable for a minimum fine rupees one thousand for every day during which such default continues.
- (b) The company shall also be liable to pay simple interest at the rate of 18% p.a. during the period for which such default continues.
- (c) Equality of burden is the basis of Co-suretyship. This is contained in section 146 of the Indian Contract Act, 1872, 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 Pawan in payment, Tarun cannot escape from his liability. All the three sureties Suraj, Tarun and Usha are liable to pay equally, in absence of any contract between them.

- (d) According to section 40 of the Negotiable Instruments Act, 1881,

Where the holder of a negotiable instrument—

- without the consent of the indorser,
- destroys or impairs the indorser’s remedy against a prior party,

the indorser is discharged from liability to the holder to the same extent as if the instrument had been paid at maturity.

In the given question, ‘M’ strikes out, without Q’s consent, the endorsements by ‘O’ and ‘P’. In the light of the above provision of law and facts of the question, ‘M’ is not entitled to recover anything from ‘Q’.

Question 2

- (a) Explain the provisions of e-voting in an annual general meeting in the following cases as per the Companies Act, 2013:
- (i) ‘A’ and his wife ‘B’ has joint Demat Account in Alfa Investment Ltd. in such a case, who will cast the vote in e-voting system?

- (ii) AGM is going to be held on 07-09-2020. Then what will be the e- voting period and the time of closing? **(4 Marks)**
- (b) Examine the validity of the following with reference to the relevant provisions of the Companies Act, 2013:
- (i) The Board of Directors of a company refuse to convene the extraordinary general meeting of the members on the ground that the requisitionists have not given explanatory statement for the resolution proposed to be passed at the meeting.
 - (ii) The Board of Directors refuse to convene the extraordinary general meeting on the ground that the requisitions have not been signed by the joint holder of the shares.
 - (iii) Adjournment of extraordinary general meeting called upon the requisition of members on the ground that the quorum was not present in the meeting. **(6 Marks)**
- (c) Shyam, at the request of Govind, sells goods which were, in the possession of Govind. However, Govind had no right to dispose of such goods. Shyam did not know this and handed over the proceeds of the sale to Govind. Afterwards, Manohar, who was the true owner of the goods, sued Shyam and recovered the value of the goods. In the light of the provisions of the Indian Contract Act, 1872, answer the following questions:
- (i) Is Govind liable to indemnify Shyam for his payment to Manohar?
 - (ii) What will be the liability of Govind if the goods are a prohibited drug? **(4 Marks)**
- (d) A is a payee and holder of a bill of exchange. He endorses it in blank and delivers it to B. B endorses it in full to C or order. C without endorsement transfers the bill to D. State giving reasons whether D, as bearer of the bill of exchange, is entitled to recover the payment from A or B or C. **(3 Marks)**

Answer

- (a) (i) **Joint shareholders must concur in voting unless the articles provide to the contrary.**

The voting in case of joint shareholders is done in the order of seniority, which is determined on the basis of the order in which their names appear in the register of members/ shareholders. The joint- holders have a right to instruct the company as to the order in which their names are to appear in the register.

As per Rule 21 of the Companies (Management and Administration) Rules, 2014, the Scrutinizers shall arrange for Polling papers and distribute them to the members and proxies present at the meeting; in case of joint shareholders, the polling paper shall be given to the first named holder or in his absence to the joint holder attending the meeting as appearing in the chronological order in the folio.

Thus, in the given case, 'A' or his wife 'B', whosoever names appears first in chronological order in the register of members/ shareholders shall be entitled to vote.

- (ii) **Time period for e-voting:** The facility for remote e-voting shall remain open for not less than three days and shall close at 5.00 p.m. on the date preceding the date of the general meeting.

Thus, if the Annual General Meeting is going to be held on 7.9.2020, the facility for remote e- voting shall open on 4.9.2020 and close at 5.00 p.m. on 6.9.2020.

- (b) (i) Rule 17 of the Companies (Management and Administration) Rules, 2014 provides that no explanatory statement as required under section 102 of the Companies Act, 2013, need be annexed to the notice of an extraordinary general meeting convened by the requisitionists and the requisitionists may disclose the reasons for the resolution(s) which they propose to move at the meeting.

Hence, the Board of Directors cannot refuse to convene the extraordinary general meeting of the members on the ground that the requisitionists have not given the explanatory statement for the resolution proposed to be passed at the meeting.

- (ii) The notice shall be signed by all the requisitionists or by a requisitionists duly authorised in writing by all other requisitionists on their behalf or by sending an electronic request attaching therewith a scanned copy of such duly signed requisition.

Hence, it is imperative for joint holders (or by requisitionist duly authorised in writing by joint holder) also to sign the notice to call the meeting. Thus, Board of directors are correct in refusing to convene the extra ordinary general meeting on the ground that the requisitions have not been signed by the joint holder of shares.

- (iii) According to section 103(2)(b) of the Companies Act, 2013, if the quorum is not present within half-an-hour from the time appointed for holding a meeting of the company the meeting, if called by requisitionists under section 100, shall stand cancelled.

Thus, if quorum is not present for the meeting called by requisitionists, it shall stand cancelled and cannot be adjourned.

- (c) According to section 178 of the Indian Contract Act, 1872, where a mercantile agent is, with the consent of the owner, in possession of goods or the documents of title to goods, any pledge made by him, when acting in the ordinary course of business of a mercantile agent, shall be as valid as if he were expressly authorised by the owner of the goods to make the same; provided that the pawnee acts in good faith and has not at the time of the pledge notice that the Pawnor has no authority to pledge.

It is also to be noted that:

1. The possession of goods must be with the consent of the owner. If possession has been obtained dishonestly or by a trick, a valid pledge cannot be effected.
2. The pledgee should have no notice of the pledger's defect of title. If the pledgee knows that the pledger has a defective title, the pledge will not be valid.

- (i) In the given question, Shyam had no notice of the Govind's defect of title. He acted in ordinary course of business of a mercantile agent considering Govind as owner of the good and genuinely handed over the proceed of the sale to him. Therefore, said transaction is invalid.

Thus, Govind shall be liable to indemnify Shyam for his payment to Manohar.

- (ii) Govind shall not be liable to indemnify Shyam as selling of prohibited drugs is a prohibited act and against the public policy.
- (d) According to section 49 of the Negotiable Instruments Act, 1881, the holder of a negotiable instrument indorsed in blank may—
- without signing his own name, by writing above the endorser's signature a direction to pay to any other person as endorsee, convert the indorsement in blank into an indorsement in full; and the holder does not thereby incur the responsibility of an endorser.

According to section 55, if a negotiable instrument, after having been indorsed in blank, is indorsed in full, the amount of it cannot be claimed from the endorser in full, except by the person to whom it has been indorsed in full, or by one who derives title through such person.

As per the facts of the question and above mentioned provisions of the Negotiable Instruments Act, 1881, D as the bearer of the Bill of Exchange, is entitled to receive payment or to sue drawer, acceptor, or A who indorsed the bill in blank, but he cannot sue B or C.

Question 3

- (a) (i) *RD Ltd. issued a prospectus. All the statements contained therein were literally true. It also stated that company had paid dividends for a number of years but did not disclose the fact that the dividends were not paid out of trading profits but out of capital profits. An allottee of shares claims to avoid the contract on the ground that the prospectus was false in material particulars. Decide that the argument of shareholder, as per the provision of the Companies Act, 2013, is correct or not?*

(3 Marks)

- (ii) *Define "Small Company".*

(2 Marks)

- (b) *Referring the provisions of the Companies Act, 2013, regarding appointment of auditors, answer the following:*

- (i) *XYZ Ltd. is a newly established company owned by the Central Government. State the provisions regarding appointment of its first auditor.*

- (ii) *Mr. Kamal is the auditor of XYZ Limited, which is a Government company. He has resigned on 31st December, 2020 while the financial year of the company ends on 31st March, 2021. Explain the provisions regarding filling or such vacancy. Would your answer differ if it is other than a Government company?*

(5 Marks)

- (c) Referring the provisions of the Negotiable Instruments Act, 1881 give the answer of the following.
- (i) A promissory note was made without mentioning any time for payment. The holder added the words 'on demand' on the face of the instrument. Whether this may be treated as material alteration in the instrument?
 - (ii) Ankit draws a cheque for ₹ 2,000 and hands it over to Shreya by way of gift. Whether Shreya is a holder in due course? **(4 Marks)**
- (d) Explain the Mischief Rule / the rule in Heydon's case for interpretation of statute. Also give four matters it considers in construing an Act. **(3 Marks)**

Answer

- (a) (i) According to section 34 of the Companies Act, 2013, where a prospectus, issued, circulated or distributed, includes any statement which is untrue or misleading in form or context in which it is included or where any inclusion or omission of any matter is likely to mislead, every person who authorises the issue of such prospectus shall be liable under section 447.

Further, Section 35(3) provides that, where it is proved that a prospectus has been issued with intent to defraud the applicants for the securities of a company or any other person or for any fraudulent purpose, every person referred to in sub-section (1) of section 35, shall be personally responsible, without any limitation of liability, for all or any of the losses or damages that may have been incurred by any person who subscribed to the securities on the basis of such prospectus.

In the given question, the non-disclosure of the fact that dividends were paid out of capital profits is a concealment of material fact as a company is normally required to distribute dividend only from trading or revenue profits and under exceptional circumstances it can pay dividend out of capital profits. Hence, a material misrepresentation has been made.

Accordingly, in the given case the allottee can avoid the contract of allotment of shares.

- (ii) According to section (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 profit and loss account for the immediately preceding financial year does not exceed two crore rupees or such higher amount as may be prescribed which shall not be more than one hundred crore rupees:

Provided that 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.

(b) (i) First auditor

- (1) According to section 139(7) of the Companies Act, 2013, in the case of a Government company or any other company owned or controlled, directly or indirectly, by the Central Government, or by any State Government, or Governments, or partly by the Central Government and partly by one or more State Governments, the first auditor shall be appointed by the Comptroller and Auditor General of India (CAG) within 60 days from the date of registration of the company.
- (2) In case the CAG does not appoint first auditor within the said period, the Board of Directors of the company shall appoint such auditor within the next 30 days.
- (3) Further, in the case of failure of the Board to appoint such auditor within the next 30 days, it shall inform the members of the company who shall appoint such auditor within the 60 days at an Extraordinary General Meeting, who shall hold office till the conclusion of the first annual general meeting.

XYZ Ltd. can follow the above provisions for appointment of its first auditor.

(ii) Casual vacancy

According to section 139(8) of the Companies Act, 2013,

- (1) In the case of a company whose accounts are subject to audit by an auditor appointed by the CAG, casual vacancy of an auditor shall be filled by the CAG within 30 days.
- (2) In case the CAG does not fill the vacancy within the said period, the Board of Directors shall fill the vacancy within next 30 days.

XYZ Ltd. can follow the above provisions for filling of its casual vacancy of its auditor.

In case, XYZ Ltd. would have been a company other than a government company, the following provisions would be applicable for filling of its casual vacancy:

- (a) The Board may fill any casual vacancy in the office of an auditor within 30 days but where such vacancy is caused by the resignation of an auditor, such

appointment shall also be approved by the company at a general meeting convened within three months of the recommendation of the Board.

- (b) Any auditor appointed in a casual vacancy shall hold office until the conclusion of the next annual general meeting.

- (c) (i) **Material alteration:** An alteration is material which in any way alters the operation of the instrument and affects the liability of parties thereto.

Any alteration is material

- (a) which alters the business effect of the instrument if used for any business purpose;
- (b) which causes it to speak a different language in legal effect from that which it originally spoke or which changes the legal identity or character of the instrument.

The following alterations are specifically declared to be material: any alteration of (i) the date, (ii) the sum payable, (iii) the time of payment, (iv) the place of payment, or the addition of a place of payment.

A promissory note was made without mentioning any time for payment. The holder added the words "on demand" on the face of the instrument. As per the above provision of the Negotiable Instruments Act, 1881 this is not a material alteration as a promissory note where no date of payment is specified will be treated as payable on demand. Hence, adding the words "on demand" does not alter the business effect of the instrument.

- (ii) **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.

Person holder in due course: Holder in due course means any person who for consideration became the possessor of a promissory note, bill of exchange or cheque (if payable to bearer) or the payee or endorsee thereof (if payable to order) before the amount mentioned in it became payable, and without having sufficient cause to believe that any defect existed in title of the person from whom he derived his title.

In the given case, Ankit draws a cheque for ₹ 2,000 and hands it over to Shreya by way of gift. Hence, Shreya can be termed as a holder because she has a right to possession and to receive the amount due in her own name.

But she cannot be termed as a holder in due course.

(d) **Mischief Rule/ Heydon's Rule:** Where the language used in a statute is capable of more than one interpretation, the most firmly established rule for construction is the principle laid down in the Heydon's case. This rule enables, consideration of four matters in constituting an Act:

- (1) what was the law before making of the Act,
- (2) what was the mischief or defect for which the law did not provide,
- (3) what is the remedy that the Act has provided, and
- (4) what is the reason for the remedy.

The rule then directs that the courts must adopt that construction which 'shall suppress the mischief and advance the remedy'. Therefore, even in a case where the usual meaning of the language used falls short of the whole object of the legislature, a more extended meaning may be attributed to the words, provided they are fairly susceptible of it. If the object of any enactment is public safety, then its working must be interpreted widely to give effect to that object. Thus, in the case of Workmen's Compensation Act, 1923 the main object being provision of compensation to workmen, it was held that the Act ought to be so construed, as far as possible, so as to give effect to its primary provisions.

However, it has been emphasized by the Supreme Court that the rule in Heydon's case is applicable only when the words used are ambiguous and are reasonably capable of more than one meaning [*CIT v. Sodra Devi* (1957) 32 ITR 615 (SC)].

Question 4

- (a) (i) *Diya Limited, incorporated under the provisions of the Companies Act, 2013, has two subsidiaries – Jai Limited and Vijay Limited. All the three companies have prepared their financial statements for the year ended 31st March, 2021. Examining the provisions of the Companies Act, 2013, explain in what manner the subsidiaries– Jai Limited and Vijay Limited shall prepare their Balance Sheet and Statement of Profit & Loss?* **(3 Marks)**
- (ii) *The Companies Act, 2013 has prescribed an additional duty on the Board of directors to include in the Board's Report a 'Directors' Responsibility Statement'. Briefly explain any three matters to be furnished in the said statement.* **(3 Marks)**
- (b) *What are provisions of the Companies Act, 2013 relating to the appointment of 'Debenture Trustee' by a company? Whether the following can be appointed as 'Debenture Trustee'?*
- (i) *A shareholder of the company who has shares of ₹ 10,000.*
 - (ii) *A creditor whom the company owes ₹ 999 only.*
 - (iii) *A person who has given a guarantee for repayment of amount of debentures issued by the company.* **(4 Marks)**

- (c) A confusion, regarding the meaning of 'financial year' arose among the financial executive and accountant of a company. Both were having different arguments regarding the meaning of financial year & calendar year. What is the correct meaning of financial year under the provision of the General Clauses Act, 1897? How it is different from calendar year? **(4 Marks)**
- (d) In what way are the following terms considered as external aid in the interpretation of statutes:
- (i) Historical Setting
 - (ii) Use of Foreign Decisions **(3 Marks)**

Answer

- (a) (i) According to section 129(3) of the Companies Act, 2013, where a company has one or more subsidiaries or associate companies, it shall, in addition to financial statements provided under sub-section (2), prepare a consolidated financial statement (CFS) of the company and of all the subsidiaries and associate companies in the same form and manner as that of its own and in accordance with applicable accounting standards, which shall also be laid before the annual general meeting of the company along with the laying of its financial statement under sub-section (2).

The company shall also attach along with its financial statement, a separate statement containing the salient features of the financial statement of its subsidiary or subsidiaries and associate company or companies in Form AOC-1 as per Rule 5 of the Companies (Accounts) Rules, 2014.

Provided further that the Central Government may provide for the consolidation of accounts of companies in such manner as may be prescribed under Rule 6 of the Companies (Accounts) Rules, 2014.

Since, consolidation of accounts is to be done by the holding company (i.e. Diya Limited), Jai Limited and Vijay Limited shall prepare their Balance Sheet and Statement of Profit and Loss Account normally following the relevant provisions of the Companies Act, 2013 compliant with the applicable Accounting Standards.

- (ii) **Directors' Responsibility Statement:** According to section 134(5) of the Companies Act, 2013, the Directors' Responsibility Statement referred to in 134(3)(c) shall state that—
- (1) in the preparation of the annual accounts, the applicable accounting standards had been followed along with proper explanation relating to material departures;
 - (2) the directors had selected such accounting policies and applied them consistently and made judgments and estimates that are reasonable and prudent so as to give a true and fair view of the state of affairs of the company

at the end of the financial year and of the profit and loss of the company for that period;

- (3) the directors had taken proper and sufficient care for the maintenance of adequate accounting records in accordance with the provisions of this Act for safeguarding the assets of the company and for preventing and detecting fraud and other irregularities;
- (4) the directors had prepared the annual accounts on a going concern basis; and
- (5) the directors, in the case of a listed company, had laid down internal financial controls to be followed by the company and that such internal financial controls are adequate and were operating effectively.

Here, the term “internal financial controls” means the policies and procedures adopted by the company for ensuring the orderly and efficient conduct of its business, including adherence to company's policies, the safeguarding of its assets, the prevention and detection of frauds and errors, the accuracy and completeness of the accounting records, and the timely preparation of reliable financial information;

- (6) the directors had devised proper systems to ensure compliance with the provisions of all applicable laws and that such systems were adequate and operating effectively.

- (b) **Appointment of Debenture Trustee:** Under section 71 (5) of the Companies Act, 2013, no company shall issue a prospectus or make an offer or invitation to the public or to its members exceeding five hundred for the subscription of its debentures, unless the company has, before such issue or offer, appointed one or more debenture trustees and the conditions governing the appointment of such trustees shall be such as may be prescribed.

Rule 18 (2) of the Companies (Share Capital and Debentures) Rules, 2014, framed under the Companies Act for the issue of secured debentures provide that before the appointment of debenture trustee or trustees, a written consent shall be obtained from such debenture trustee or trustees proposed to be appointed and a statement to that effect shall appear in the letter of offer issued for inviting the subscription of the debentures.

Further according to the provided rules *inter-alia*, no person shall be appointed as a debenture trustee, if he-

- (1) beneficially holds shares in the company;
- (2) is beneficially entitled to moneys which are to be paid by the company otherwise than as remuneration payable to the debenture trustee;
- (3) has furnished any guarantee in respect of the principal debts secured by the debentures or interest thereon;

Thus, based on the above provisions answers to the given questions are as follows:

- (i) A shareholder who has holds shares of ₹ 10,000, cannot be appointed as a debenture trustee.
 - (ii) A creditor whom company owes ₹ 999 cannot be appointed as a debenture trustee. The amount owed is immaterial.
 - (iii) A person who has given guarantee for repayment of principal and interest thereon in respect of debentures also cannot be appointed as a debenture trustee.
- (c) **Financial Year:** According to Section 3(21) of the General Clauses Act, 1897, financial year shall mean the year commencing on the first day of April.

The term Year has been defined under section 3(66) as a year reckoned according to the British calendar. Thus, as per the General Clauses Act, 1897, year means calendar year which starts from January to December.

Difference between Financial Year and Calendar Year: Financial year starts from first day of April but Calendar Year starts from first day of January.

- (d) (i) **Historical Setting:** The history of the external circumstances which led to the enactment in question is of much significance in construing any enactment. We have, for this purpose, to take help from all those external or historical facts which are necessary in the understanding and comprehension of the subject matter and the scope and object of the enactment. History in general and Parliamentary History in particular, ancient statutes, contemporary or other authentic works and writings all are relevant in interpreting and construing an Act.
- (ii) **Use of Foreign Decisions:** Foreign decisions of countries following the same system of jurisprudence as ours and given on laws similar to ours can be legitimately used for construing our own Acts. However, prime importance is always to be given to the language of the Indian statute. Further, where guidance can be obtained from Indian decisions, reference to foreign decisions may become unnecessary.

Question 5

- (a) *Examine that following offers of ABC Limited are in compliance with provisions of the Companies Act, 2013, related to private placement or should these offers be treated as public:*
- (i) *ABC limited wants to raise funds for its upcoming project. It has issued private placement offer letters to 55 persons in their individual name to issue its equity shares. Out of these four are qualified institutional buyers.*
 - (ii) *If in case (i) before allotment under this offer letter company issued another private placement offer to another 155 persons in their individual name for issue of its debentures.*

(iii) Being a public company can it issue securities in a private placement offers?

(5 Marks)

(b) Discuss the following situations in the light of 'Deposit provisions' as contained in the Companies Act, 2013 and the Companies (Acceptance of Deposits) Rules, 2014, as amended from time to time.

(i) Bhupendra, one of the Directors of Moon Technology Private Limited, a start-up company, requested his close friend Paras to lend to the company ₹ 20.00 lacs in a single tranche by way of a convertible note repayable within a period of six years from the date of its issue. Advise whether it is a deposit or not.

(ii) Shriram Readymade Garments Limited wants to accept deposits of ₹ 50.00 lacs from its member for tenure, which is less than six months. Is there any possibility to do so?

(iii) The turnover of Y Ltd. is ₹ 400 crore as per last audited financial statement and net worth is ₹ 50 crores. Can Y Ltd. accept deposits from the public as per section 73 of the Companies Act, 2013?

(5 Marks)

OR

New Pharma Ltd. issued a notice for holding its annual general meeting on 7th September 2020. The notice was posted to the members on 16th August 2020. Some members of the company alleged that the company has not complied with the provision of the Companies Act, 2013, with regard to the period of notice and as such the meeting was invalid. Referring to the provision of the Companies Act, 2013, decide:

(i) Whether meeting has been validly called?

(ii) If there is a shortfall in the notice, state and explain by how many days does the notice fall short of statutory requirements?

(iii) Whether the length of serving of notices be curtailed by Article of Association?

(c) Alpha Motor Ltd. agreed to sell a bike to Ashok under hire-purchase agreement on guarantee of Abhishek. The Terms were: hire-purchase price ₹ 96,000 payable in 24 monthly instalments of ₹ 8,000 each. Ownership to be transferred on the payment of last instalment. State whether Abhishek is discharged in each of the following alternative case under the provisions of the Indian Contract Act, 1872:

(i) Ashok paid 12 instalments but failed to pay next two instalments. Alpha Motor Ltd. sued Abhishek for the payment of arrears and Abhishek paid these two instalments i.e. 13th and 14th. Abhishek then gave a notice to Alpha Motor Ltd. to revoke his guarantee for the remaining months.

(ii) If after 15th months, Abhishek died due to COVID-19.

(4 Marks)

(d) Give the definition of the following as per the General Clauses Act, 1897:

- (i) "Rule"
- (ii) "Oath"
- (iii) "Person"

(3 Marks)

Answer

- (a) According to section 42 of the Companies Act, 2013 any private or public company may make private placement through issue of a private placement offer letter.

However, the offer shall be made to the persons not exceeding fifty or such higher number as may be prescribed, in a financial year. For counting number of persons, Qualified Institutional Buyers (QIBs) and employees of the company being offered securities under a scheme of employees' stock option will not be considered.

Further, Rule 14 (2) of the Companies (Prospectus and Allotment of Securities) Rules, 2014 prescribes maximum of 200 persons who can be offered securities under the private placement in a financial year, though this limit should be counted separately for each type of security.

It is to be noted that if a company makes an offer or invitation to more than the prescribed number of persons, it shall be deemed to be an offer to the public and accordingly, it shall be governed by the provisions relating to prospectus.

Also, a company is not permitted to make fresh offer under this section if the allotment with respect to any offer made earlier has not been completed or otherwise, that offer has been withdrawn or abandoned by the company. This provision is applicable even if the issue is of different kind of security.

Any offer or invitation not in compliance with the provisions of this section shall be treated as a public offer and all provisions will apply accordingly.

- (i) In the given case ABC Limited, though is a public company but the private placement provisions allow even a public company to raise funds through this route. The company has given offer to 55 persons out of which 4 are qualified institutional buyers and hence, the offer is given effectively to only 51 persons which is well within the limit of 200 persons. From this point of view, the company complies the private placement provisions.

- (ii) However, as per the question, the company has given another private placement offer of debentures before completing the allotment in respect of first offer and therefore, the second offer does not comply with the provisions of section 42. Hence, the offers given by the company will be treated as public offer.

In case the company gives offer for debentures in the same financial year after allotment of equity shares is complete then both the offers can well be treated as private placement offers.

- (iii) According to section 42 of the Companies Act, 2013 any private or public company may make private placement through issue of a private placement offer letter. Hence, ABC Limited can issue securities in a private placement offer.
- (b) (i) In terms of Rule 2 (1)(c)(xvii) of the Companies (Acceptance of Deposits) Rules, 2014, if a start-up company receives rupees twenty-five lakh or more by way of a convertible note (convertible into equity shares or repayable within a period not exceeding ten years from the date of issue) in a single tranche, from a person, it shall not be treated as deposit.

In the given case, Moon Technology Private Limited, a start-up company, received ₹ 20.00 lacs from Paras in a single tranche by way of a convertible note which is repayable within a period of six years from the date of its issue. The amount received is below threshold limit of ₹ 25.00 lacs. Hence, the amount of ₹ 20.00 lacs shall be considered as deposit and the provisions for acceptance of deposit will apply accordingly.

- (ii) According to Rule 3 (1) of the Companies (Acceptance of Deposits) Rules, 2014, a company is not permitted to accept or renew deposits (whether secured or unsecured) which is repayable on demand or in less than six months. Further, the maximum period of acceptance of deposit cannot exceed thirty six months.

However, as an exception to this rule, for the purpose of meeting any of its short-term requirements of funds, a company is permitted to accept or renew deposits for repayment earlier than six months subject to the conditions that:

- (1) such deposits shall not exceed ten per cent. of the aggregate of the paid-up share capital, free reserves and securities premium account of the company; and
- (2) such deposits are repayable only on or after three months from the date of such deposits or renewal.

In the given case of Shriram Readymade Garments Limited, it wants to accept deposits of ₹ 50.00 lacs from its members for a tenure which is less than six months. It can do so if it justifies that the deposits are required for the purpose of meeting any of its short-term requirements of funds but in no case such deposits shall exceed 10% ten per cent of the aggregate of its paid-up share capital, free reserves and securities premium account and further, such deposits shall be repayable only on or after three months from the date of such deposits.

- (iii) As per Rule 2 (1) (e) of the Companies (Acceptance of Deposits) Rules, 2014, the term “eligible company” means a public company as referred to in section 76 (1), having a net worth of not less than one hundred crore rupees or a turnover of not less than five hundred crore rupees and which has obtained the prior consent in general meeting by means of a special resolution and also filed the said resolution with the Registrar of Companies before making any invitation to the public for acceptance of deposits:

However, an eligible company, which is accepting deposits within the limits specified under section 180 (1) (c), may accept deposits by means of an ordinary resolution.

Thus, a public company can accept deposit from public if it is an eligible company.

In the given question, Y Ltd. has a turnover of ₹ 400 crore and net worth of ₹ 50 crore. Hence, it cannot be termed as an eligible company and thus can not accept deposits from the public.

OR

According to section 101(1) of the Companies Act, 2013, a general meeting of a company may be called by giving not less than clear twenty-one days' notice either in writing or through electronic mode in such manner as may be prescribed.

Also, it is to be noted that 21 clear days mean that the date on which notice is served and the date of meeting, are excluded for sending the notice.

Further, Rule 35(6) of the Companies (Incorporation) Rules, 2014, provides that in case of delivery by post, such service shall be deemed to have been effected-in the case of a notice of a meeting, at the expiration of forty eight hours after the letter containing the same is posted.

Hence, in the given question:

- (i) A 21 days' clear notice must be given. In the given question, only 19 clear days' notice is served (after excluding 48 hours from the time of its posting and the day of sending and date of meeting). Therefore, the meeting was not validly called.
 - (ii) As explained in (i) above, notice falls short by 2 days.
 - (iii) The Companies Act, 2013 does not provide anything specific regarding the condonation of delay in giving of notice. Hence, the delay in giving the notice calling the meeting cannot be condoned.
- (c) According to section 130 of the Indian Contract Act, 1872, the continuing guarantee may at any time be revoked by the surety as to future transactions by notice to the creditors. Once the guarantee is revoked, the surety is not liable for any future transaction however he is liable for all the transactions that happened before the notice was given.

A specific guarantee can be revoked only if liability to principal debtor has not accrued.

- (i) In the given question Ashok paid 12 instalments (out of total 24 monthly instalments), but failed to pay next two instalments. Abhishek (guarantor) paid the 13th and 14th instalments but then he revoked guarantee for the remaining months. Thus, Abhishek is not liable for instalments that was made after the notice, but he is liable for instalments made before the notice (which he had paid i.e. 13th and 14th instalments).

- (ii) According to section 131 of the Indian Contract Act, 1872, in the absence of any contract to the contrary, the death of surety operates as a revocation of a continuing guarantee as to the future transactions taking place after the death of surety. However, the surety's estate remains liable for the past transactions which have already taken place before the death of the surety.

In the given question, Abhishek (guarantor) died after 15th month. This will operate as a revocation of a continuing guarantee as to the future transactions taking place after the death of surety (i.e. Abhishek). However, the Abhishek's estate remains liable for the past transactions (i.e. 15th month and before) which have already taken place before the death of the surety.

- (d) (i) **Rule:** As per section 3(51) of the General Clauses Act, 1897, 'Rule' shall mean a rule made in exercise of a power conferred by any enactment, and shall include a Regulation made as a rule under any enactment.
- (ii) **Oath:** As per section 3(37) of the General Clauses Act, 1897, 'Oath' shall include affirmation and declaration in the case of persons by law allowed to affirm or declare instead of swearing.
- (iii) **Person:** As per section 3(42) of the General Clauses Act, 1897, "Person" shall include:
- (1) any company, or
 - (2) association, or
 - (3) body of individuals, whether incorporated or not.