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COMPANY LAW

B.C.O.C.-135

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By: Harish Arora



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**Sample Preview
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QUESTION PAPER

June – 2023

(Solved)

COMPANY LAW

B.C.O.C.-135

Time: 3 Hours]

[Maximum Marks: 100

Note: Answer any five questions. All questions carry equal marks.

Q. 1. Define a public company. Distinguish between a public company and a private company. What are the steps necessary for conversion of private company into public company?

Ans. Ref.: See Chapter-2, Page No. 17, Q. No. 2, Page No. 16, 'Distinction between a Private Company and Public Company' and Page No. 19, Q. No. 3.

Q. 2. What is the meaning and purpose of Memorandum of Association? Explain the various clauses which are included in the Memorandum of Association.

Ans. Ref.: See Chapter-6, Page No. 48, Q. No. 1, Q. No. 2 and Q. No. 3.

Q. 3. (a) What is Deemed Prospectus? What are the provisions of the Companies Act, 2013 with respect to deemed prospectus?

Ans. Ref.: See Chapter-8, Page No. 69, Q. No. 7.

(b) Explain shelf prospectus and red herring prospectus.

Ans. Ref.: See Chapter-8, Page No. 68, Q. No. 6.

Q. 4. Explain the meaning, features and different types of debentures.

Ans. Ref.: See Chapter-9, Page No. 78, Q. No. 7 and Page No. 79, Q. No. 8.

Q. 5. What is allotment of shares? Explain the general and legal rules for the allotment of shares.

Ans. Ref.: See Chapter-10, Page No. 85, 'Allotment of Shares'.

Q. 6. (a) Differentiate between transfer and transmission of shares.

Ans. Ref.: See Chapter-11, Page No. 103, Q. No. 6.

(b) Explain the various ways when a person may cease to be a member of a company.

Ans. Ref.: See Chapter-12, Page No. 106, 'Termination of Membership' and Page No. 108, Q. No. 4.

Q. 7. Explain the liabilities of directors towards company, towards third party and criminal liability.

Ans. Ref.: See Chapter-13, Page No. 121, Q. No. 9.

Q. 8. (a) Explain the different types of resolutions. For what purposes such resolutions are necessary?

Ans. Ref.: See Chapter-16, Page No. 137, 'Resolutions'.

(b) Explain the rules regarding notice of general meeting.

Ans. Ref.: See Chapter-16, Page No. 141, Q. No. 3.

Q. 9. Write short notes on the following:

(a) Winding up of a company

Ans. Ref.: See Chapter-20, Page No. 156, 'Meaning of Winding Up' and 'Modes of Winding Up'.

(b) Interim dividend

Ans. Ref.: See Chapter-17, Page No. 144, 'Interim Dividend' and Page No. 146, Q. No. 4.

(c) Position of a Company Secretary

Ans. Ref.: See Chapter-15, Page No. 131, Q. No. 3.

(d) Doctrine of Indoor Management

Ans. Ref.: See Chapter-7, Page No. 55, 'Doctrine of Indoor Management'.



QUESTION PAPER

December – 2022

(Solved)

COMPANY LAW

B.C.O.C.-135

Time: 3 Hours]

[Maximum Marks: 100

Note: Answer any five questions. All questions carry equal marks.

Q. 1. (a) Describe the main characteristics of a company.

Ans. Ref.: See Chapter-1, Page No. 11, Q. No. 2.

(b) Distinguish between company and limited liability partnership.

Ans. Ref.: See Chapter-1, Page No. 4, 'Distinction between Company and Limited Liability Partnership'.

Q. 2. Explain the duties and liabilities of a promoter.

Ans. Ref.: See Chapter-3, Page No. 22, 'Duties of a Promoter and Liabilities of a Promotion'.

Q. 3. Explain the meaning and purpose of Articles of Association. Discuss the binding effect of Memorandum and Articles. How far are they binding on outsiders?

Ans. Ref.: See Chapter-7, Page No. 52, 'Meaning and Purpose of Articles', Page No. 54, 'Binding Effect of Memorandum and Articles' and Page No. 57, Q. No. 4.

Q. 4. What is transfer of shares? Explain the procedure for effecting transfer of shares. Discuss the power of the Board of Directors to refuse the registration of transfer of shares.

Ans. Ref.: See Chapter-11, Page No. 97, 'Procedure of Transfer of Shares'.

Q. 5. Who is a director of a company? Who can be appointed as a director of a company? Explain the qualifications and disqualifications of a director.

Ans. Ref.: See Chapter-13, Page No. 110, 'Introduction', 'Definition of a Director', 'Who can be Appointed as a Director?', 'Position of Directors' and Page No. 111, 'Qualifications of a Director' and 'Disqualifications of Directors'.

Q. 6. (a) What is managerial remuneration? What is not included in the managerial remuneration?

Ans. Ref.: See Chapter-10, Page No. 125, Q. No. 1, Page No. 124, 'Meaning of Managerial Remuneration' and 'What is not Managerial Remuneration?'

(b) Discuss the provisions relating to payment of dividend.

Ans. Ref.: See Chapter-17, Page No. 144, 'Payment of Dividend' and Page No. 146, Q. No. 1.

Q. 7. (a) Discuss the inspection of Books of Accounts of a company. Who are the persons responsible for keeping books of accounts and what is the punishment for not keeping proper books of accounts?

Ans. Ref.: See Chapter-18, Page No. 148, 'Inspection of Books of Account'.

(b) Who cannot be appointed as an auditor?

Ans. Ref.: See Chapter-19, Page No. 151, 'Appointment of an Auditor'.

Q. 8. What is winding-up of a company? How is it different from dissolution? Explain the procedure for winding-up of a company.

Ans. Ref.: See Chapter-20, Page No. 156, 'Meaning of Winding-up' and Page No. 157, 'Procedure for Winding up'.

Q. 9. Write short notes on the following:

(a) National Company Law Appellate Tribunal

Ans. Ref.: See Chapter-5, Page No. 36, 'National Company Law Tribunal'.

(b) Formation of a company

Ans. Ref.: See Chapter-6, Page No. 32, Q. No. 1.

(c) Doctrine of Indoor Management

Ans. Ref.: See Chapter-7, Page No. 55, 'Doctrine of Indoor Management'.

(d) Sweat equity shares

Ans. Ref.: See Chapter-9, Page No. 73, 'Sweat Equity Shares'.



Sample Preview of The Chapter

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COMPANY LAW

BLOCK-I : COMPANY AND ITS FORMATION

Nature and Types of Companies



INTRODUCTION

In most of the Companies, investment is done by a large number of investors, known as its shareholders who live/work at different geographical places within the country or even abroad. Due to this reason, they cannot themselves manage the affairs of their company. Therefore, to safeguard their interests, monitoring/ regulation of the affairs of the Companies is done by the Government. The Companies Act, 2013 (amended in 2015, 2017 & 2019), contains rules concerning the formation, management, administration and winding up of companies. As against the earlier, Companies Act, 1956 which was having 658 sections and XV schedules, The Companies Act, 2013 has 470 sections and VII schedules.

CHAPTER AT A GLANCE

MEANING AND DEFINITION OF A COMPANY

Company is an association of persons formed for a common purpose, economic or non-economic. As per law, every company is incorporated under the Companies Act and therefore, partnership firm is not a company because it is not registered under the Companies Act or under any previous company law. A company is an incorporated association which is an artificial person created by law, having a separate entity, with a perpetual succession and a common seal.

COMPANY VS. BODY CORPORATE

Section 2 (11) of the Companies Act, 2013 says that a body corporate or Corporation includes a company incorporated outside India, but does not include a co-operative society registered under any law relating to co-operative societies; and any other body corporate (not being a company as defined in this Act), which the Central Government may, by notification, specify in this behalf. A corporation sole is a body corporate constituted in a single person who

(President, Governor) has a corporate status in right of some office or function. Companies Act does not consider a corporation sole as a body corporate but still, it is a legal person. A corporation aggregate includes a group of persons united together to form a single person. Company incorporated outside India is considered a body corporate and many provisions of the Companies Act, 2013 apply to them. In this way, corporation, or body corporate is a wider term.

IS COMPANY A CITIZEN

A Company is an artificial/legal person still it is not considered as a citizen under the Constitution of India or the Citizenship Act, 1955. In *State Trading Corporation Ltd. vs. CTO*, the Supreme Court of India has held, that a corporation including a company cannot have the status of a citizen under the Constitution of India. In this way, our Constitution does not provide for granting fundamental rights to a company which are available to citizens but, still, a company can claim the protection of the fundamental rights which are available to all persons (like the right to own property), whether citizens or not. Even as an aggregate of citizens, a company cannot have claim to fundamental rights and upon forming a company, its business is not considered to be the business of the individual citizens but it is that of the company. Still a company has a nationality, domicile and residence of the country of its incorporation.

MAIN FEATURES OF A COMPANY

- 1. Artificial Person:** Every company is formed after legal procedure and it is considered to be an artificial person in the eyes of law.
- 2. Created by Law:** A company is created by law after its registration under the Companies Act. It is an association of persons.
- 3. Separate Legal Entity:** Law treats the company as a separate entity from its members or persons who had formed it and it has the name given in the

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Memorandum of Association. The entity of the corporation is entirely separate from that of its shareholders; it bears its own name and has a seal of its own; its assets are separate and distinct from those of its members; it can sue and be sued exclusively for its own purpose. In this way, the law considers a company as an independent person distinct from its members. Just like other persons, the company can enter into a contract. The shareholders of the company are not liable for the acts done by the company nor can they be personally held, responsible for the loans taken by the company. It also follows that none of the members of the company can have the ownership on the assets of the company, individually or jointly. In the same way, lenders of the company cannot have any action against its members. The position remains the same even entire share capital of the company is directly/indirectly held by one single person.

There is a famous legal case of Salomon vs. Salomon & Co. Ltd. in this regard. One Mr. Salomon who owned a shoe business, formed a company named Salomon & Co. Ltd. in which he himself, his wife and children were shareholders. The newly formed company had taken over the shoe business of Mr. Salomon for a purchase price of £30000 comprising fully paid up shares for £20000 and debentures worth £10000 having a charge on company's assets. Mr. Salomon became the Managing Director of the company. Later, the company started facing financial difficulties. During liquidation proceedings, the assets of the company were realized for £6000. The entire sum was retained by Mr. Salomon being the secured creditor for £10000 and the unsecured creditors of £7000 did not get anything. They contended that since Mr. Salomon and Salomon & Co. Ltd. was one and the same person, their claim should be met first. It was held that Mr. Salomon was entitled to receive the amount because he was a secured creditor because it was the business of the company, not of Mr. Salomon.

4. Perpetual Succession: Members may come and go but the company goes on until it is dissolved. So, the company has a perpetual succession of a continued existence which remains unaffected by the death, insolvency, etc., of its shareholders/members.

5. Limited Liability: The liability of the shareholders of the company is limited and is there only up to the extent of their share in its capital. Companies may be classified under the following heads on the basis of liability:

- **Companies limited by Shares:** Liability of its shareholders in such companies is limited to the nominal value of shares held by them.
- **Companies limited by Guarantee:** Liability of members is limited up to the amount guaranteed by them.
- **Companies limited by guarantee but having share Capital:** Liability of members is limited to the aggregate of the amount unpaid on shares and the amount guaranteed by them.
- **Unlimited liability companies:** Liability of its members is not limited to the nominal value of the shares held, by them and they continue to be liable until every debt of the company is

repaid. But since every company has a separate legal entity, its creditors cannot bring a legal suit against its members directly.

6. Transferability of Shares: Shareholders of a company can freely transfer their shares to any person, as per the manner provided for in the Articles of the company without obtaining consent of the other members. This has been one of the prime reasons for the popularity of this form of business organization. It is possible that there may be certain restrictions imposed by the Articles of a public company as regards to transfer of its shares, but such things cannot be stopped completely. According to Section 58(2) of the Act, without prejudice to sub-section (1), the securities or other interest of any member in a public company shall be freely transferable provided that any contract or arrangement between two or more persons in respect of transfer of securities shall be enforceable as a contract. In case of a private company, there may be certain restrictions on transferability of shares even here, the right to transfer is not taken away completely.

7. Separate Property: Law says that shareholders of a company are not its part owners but they enjoy certain rights. It was held, in a case that a member does not even have an insurable interest in the property of the company (Macaura vs. Northern Assurance Co. Ltd.). Here, Macaura was having all except one share of a timber company. He got insurance of the goods of the company in his own name. When there was a loss due to fire, his claim was rejected because he had no insurable interest in the goods.

8. Common Seal: Being an artificial person, the company works through its directors, officers and other employees. The official signatures of the Company are its Common Seal. When a company has no common seal, two directors of the company can authorize or if the company has appointed a Company Secretary, then one director and the Company Secretary can authorize the transaction.

9. Company may sue and be sued in its own name: The company has a separate legal existence, it can sue and be sued in its own name, it can enter into contracts and enforce the contractual rights against others.

LIFTING THE CORPORATE VEIL

Every company is a legal entity, separate & independent from its members. Although members of the company, in fact, are its real beneficial owners of the property of the company, still, there is a line of demarcation or a veil (Covering) between the company and its members. Company enjoys several advantages due to its separate legal entity but these are available only when there is an honest use of company. In case of its fraudulent use, company's corporate veil can be lifted by law disregarding its separate entity to find the real culprits. Under the following broad circumstances, the courts may lift the corporate veil of a company:

1. Under Express Statutory Provisions: There are the following specific circumstances under the Companies Act, 2013, when directors or members of the company may be held liable personally alongwith the company:

- When there are mis-statements/misrepresentations in the prospectus issued by the company, then, the company and its directors, promoters, and persons authorized for issuing prospectus shall be liable to compensate the loss or damage to every person who subscribed for shares on the faith of untrue statement. Such persons may also be punished with imprisonment for a term which shall not be less than six months and may extend to ten years, and shall also be liable to a fine which shall not be less than the amount involved in the fraud, but which may extend to three times the amount involved in the fraud. But when such a person is able to prove that the omission was immaterial or that he had reasonable grounds to believe, and did up to the time of issue of the prospectus believe that the statement was true, he can escape the conviction.
 - When securities to the public are issued by a company, in case the minimum subscription stated in the prospectus is not received within 30 days of the issue of prospectus or such other period as may be specified by the SEBI, then the application money has to be repaid within a period of fifteen days from the closure of the issue. In case it is not done, the defaulting directors of the company shall jointly and severally be liable to repay it with interest @ 15% per annum. In case of default, the company and its officer who is in default shall be liable to a penalty of one thousand rupees for each day during which such default continues, with maximum of Rs. One lakh.
 - When an officer of the company signs documents or a contract on behalf of the company in which company's name is not mentioned/not properly mentioned, he shall be personally liable to the holder. Also, the company and its defaulting officer(s) shall be liable to a penalty of one thousand rupees for each day during which such default continues with maximum Rs. one lakh.
 - When an inspector appointed to investigate affairs of the company considers it necessary, he may investigate into the affairs of another related company in the same management or group and of any person who was its managing director or manager or employee.
 - Central Government may appoint one or more inspectors to investigate and report on matters relating to the company, and its membership for the purpose of determining the true persons financially interested in the success or failure of the company.
 - The Directors/Officers of a company will be personally liable for acts done on behalf of a company beyond the powers of the company (*ultra vires*).
 - During winding-up of a company, if it appears that any of its business has been carried on with the intention to defraud its creditors or other persons, then the persons who were knowingly party to such acts may be held, personally liable for any debts and other liabilities of the company.
 - The Directors/Officers of the company may also be held, liable personally under the provisions of other statutes such as the Income Tax Act.
- 2. Under Judicial Interpretations:** There are different cases in which the corporate veil of a company was lifted by judicial decisions under varying circumstances, some such cases are discussed as under:
- In some cases when a company was used as a medium for committing a fraud, courts had lifted its corporate veil to understand its real situation. In a case, a person was employed by the company with the agreed condition that he will not solicit company's customers or compete with it for a specific period after leaving employment. But, after leaving his job, the person formed a Company by allotting all the shares to his wife and an employee, to do the same business. The person, in fact, was controlling the new company and it was held that formation of the new company was a mere cloak so that he could break his agreement with the plaintiff. Therefore, an injunction was issued against him and the new company restraining them from soliciting customers of the plaintiff company.
 - We know that every company has a distinct entity and its affairs are managed by individuals. In a situation, it may be necessary to lift the corporate veil of a company in order to determine its enemy character and to find out persons behind the company to establish whether they are enemies or friends. In the case of Daimler Company Ltd. vs. Continental Tyre & Rubber Co. in which, a company (incorporated by a German company) was established in London for selling Germany made tyres. A majority of the shareholders and all directors of this company were Germans. A war was declared between England and Germany. Since its Board of Directors and general body of shareholders were controlled by Germans, which were the decision-making bodies, the company was held, to be a German company.
 - In one case where a transport company, which, in order to obtain licences for its vehicles, formed a subsidiary company because it could not obtain licence in its own name (Merchandise Transport Limited vs. British Transport Commission). After this, the application for licences was made in the name of the subsidiary and the vehicles were to be transferred to the subsidiary. The court rejected the application for licences and held, that the parent and the subsidiary company were one commercial unit.
 - In case, there is such arrangement existing between the shareholders and a company

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according to which the company will act as the agent of its shareholders for carrying on business, and essentially, business of the company is that of shareholders. Here, individual shareholders can be taken up for fixing their liability.

- The Courts can lift the corporate veil of a company in case of economic offences in order to bring out the real culprits. In the case of *Santanu Ray vs. Union of India*, the company allegedly had violated the provisions of the Central Excises & Salt Act, 1944. In order to find out the Directors of the company who had committed the evasion of excise duty, the court held that the veil of the corporate entity could be lifted by adjudicating authorities to determine the directors who were concerned with evasion of the excise duty and willful misstatement or suppression of facts or contravention of the provisions of the Act.
- In one case where it was observed that the only aim for forming a company was to use it as a device to reduce the amount to be paid by way of bonus to workmen, the Supreme Court upheld the piercing of the veil in order to find out the real transaction (*Workmen of Associated Rubber Industry Ltd. vs. Associated Rubber Industry Ltd.*). Here, a new company was formed without any assets except those transferred to it by the principal company. The new company did not have any business except to receive dividends on shares transferred to it by the principal company so that the later could reduce its gross profits and pay reduced bonus to the workmen. It was held, that the amount paid to the new company as dividend should be included for determining the gross profit of the principal company.
- Where a company is used for an illegal purpose, the courts have lifted its corporate veil.

DISTINCTION BETWEEN COMPANY AND PARTNERSHIP

The differences between a company and a partnership may be summarized as under:

- A minimum of two partners and maximum 50 partners have to be there in a partnership firm but in a public company there must be minimum seven members.
- There is no compulsion to register a partnership firm under Partnership Act but a company has to be registered under the Companies Act.
- A partnership firm has no legal existence apart from its partners as against a company which enjoys a legal entity separate from its members.
- Firm's partners have an unlimited liability, they are severally & jointly liable for the debts of the firm and creditors of the firm can proceed against the partners individually/collectively. But liability of shareholders of a limited liability company is limited up to the nominal value of

shares held, by them and its creditors can proceed only against the company and not against any shareholder.

- A partner cannot transfer his share in the firm without obtaining consent of other partners but shares in a public company are freely transferable.
- The death, insolvency or insanity of a member does not affect the company because it has a perpetual succession. A partnership firm gets dissolved upon such events concerning the partners until there is a contract to the contrary.
- Every company is managed by a Board of Directors who are appointed/reappointed by shareholders of the company and individual shareholders have no role in its management. But every partner can take part in the management of a firm.
- Partners act as agents of the firm as well as other partners. But, a shareholder is not an agent of the company and he cannot bind the company by his, acts.
- A partnership firm has no statutory obligations but every company has to comply with a number of statutory formalities including maintaining books, auditing of accounts, etc.
- A company can only be dissolved by following the prescribed procedure as per the Companies Act, 2013 but a partnership firm can be dissolved at any time by the partners with mutual consent.
- A company can have property in its own name and its individual shareholders do not have any legal interest in the company's property. All the partners of a firm have a joint ownership of firm's property.

DISTINCTION BETWEEN COMPANY AND LIMITED LIABILITY PARTNERSHIP

The Limited Liability Partnership (LLP) Act, 2008 permits formation of LLPs as a form of business organization which has features of both partnership and company forms. The partners of LLP have a limited liability just like shareholders of a company. The major differences between an LLP and a company are as under:

- An LLP must have minimum 2 partners without any maximum limit. A public company should have minimum 7 members and it is 2 in case of a private company with maximum 200 members.
- As per the Companies Act, name of a company must end with words Limited or Private Limited. The name of LLP must end with words LLP or Limited liability partnership.
- LLP is managed as per the agreement between its partners and the governance structure of a company is regulated by the provisions of the Companies Act through Memorandum/Articles of Association.
- Directors of a company are appointed by the shareholders who control & manage the affairs of the company. But an LLP is managed by its partners and there is no ownership-management divide.