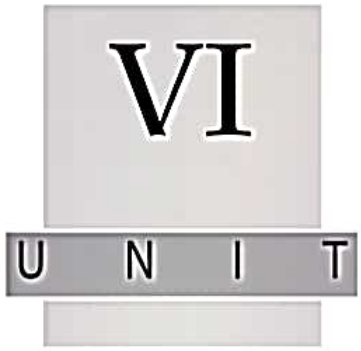

THE COMPANIES ACT, 2013

1 CHAPTER THE COMPANIES ACT, 2013

LONG ANSWER QUESTIONS:

Q.1 What is meant by lifting of corporate veil? What are the instances in which the corporate veil may be lifted?

OR

There are cases where company law disregards the principle of corporate personality or the principle that the company that the company is a legal entity distinct from its shareholders or members. Elucidate.

[Nov. 2018, 6 Marks]

OR

Explain the concept of 'Corporate Veil'. Briefly state the circumstances when the corporate veil can be lifted as per the provisions of the Companies Act, 2013. **[June 2023, 6 Marks]**

Ans. 'Lifting the veil' means looking behind the company as a legal person *i.e.*, disregarding the corporate entity and paying regard instead to the realities behind the legal form. Where the courts ignore the corporate personality and concern themselves directly with the members or directors, the corporate veil may be said to have been lifted.

The following are the cases where company law disregards the principle of corporate personality or the principle that the company is a legal entity distinct and separate from its shareholders or members:

1. **To determine the character of the company i.e. to find out whether company is an enemy or a friend:**

   The Court may rend the veil for ascertaining whether a company is an enemy company. Unlike a natural person, a company does not have mind or conscience; therefore, it cannot be a friend or foe. It may, however, be characterised as an enemy company, if its affairs are under the control of people of an enemy country. For this purpose, the Court may examine the character of the persons who are really at the helm of affairs of the company, was done in the leading case of *Daimler Co. Ltd.* vs. *Continental Tyre & Rubber Co. Ltd.*

2. Company is formed to evade taxes:

Where corporate entity is used to **evade or circumvent tax**, the Court can disregard the corporate entity **[*Juggilal* v. *Commissioner of Income Tax* AIR (SC)].**

Thus where company is used as a means of evasion of taxes, then for protection of revenue of the Government, corporate veil may be lifted. **[*Sir Dinshaw Maneckjee Petit*,** Re AIR 1927 Bom. 371].

3. Company is formed to avoid a legal obligation/welfare legislation:

Where the sole purpose for the formation of the 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 to look at the real transaction **(*The Workmen Employed in Associated Rubber Industries Limited, Bhavnagar* v. *The Associated Rubber Industries Ltd.*, Bhavnagar and another).**

4. Formation of subsidiaries to act as agents:

A company may sometimes be regarded as an agent or trustee of its members, or of another company, and may therefore be deemed to have lost its individuality in favour of its principal & the disqualifications of the principal shall be treated as that of the agent. Here the principal will be held liable for the acts of that company, as was held in the case of ***Merchandise Transport Limited* v. *British Transport Commission* (*1982*).**

5. Company formed for fraud/improper conduct or to defeat law:

The corporate veil may be lifted if the company is formed to - (*a*) defeat the law; (*b*) defraud creditors; (*c*) avoid legal obligations (arising by way of a contract). Where the device of incorporation is adopted for some illegal or improper purpose, *e.g.*, to defeat or circumvent law, to defraud creditors or to avoid legal obligations. ***[Gilford Motor Co.* v. *Horne & Jones* v. *Lipman]***

6. To determine the technical competence of the company:

A company is an artificial entity and therefore it cannot be judged for competence and experience. In some cases where the technical competence of the company is to be ascertained, such as to determine eligibility of company for certain contract, then the experience, qualification and competence of the members shall be treated as that of the company. Thus corporate veil shall be lifted as was done in the case of ***New Horizons Ltd.* v. *UOI* (1997).**

Q.2 Define OPC and state the rules regarding its membership. Can it be converted into a non-profit company under section 8 or a private company? [May 2018, 6 Marks], [RTP Nov. 2018]

Ans. One person company

Section 2(62) of the Companies Act, 2013 defines one person company (OPC) as a company which has only one person as a member. The following are the rules regarding membership of OPC:

- There can be only one person as member of OPC.
- The memorandum of OPC shall indicate the name of the other person, who shall, in the event of the subscriber's death or his incapacity to contract, become the member of the company.
- The other person whose name is given in the memorandum shall give his prior written consent in prescribed form and the same shall be filed with Registrar of companies at the time of incorporation.
- Such other person may be given the right to withdraw his consent.
- The member of OPC may at any time change the name of such other person by giving notice to the company and the company shall intimate the same to the Registrar.
- Any such change in the name of the person shall not be deemed to be an alteration of the memorandum.
- Only a natural person who is an Indian citizen whether resident in India or otherwise and has stayed in India for a period of not less than 120 days during the immediately preceding financial year-
  - shall be eligible to incorporate a OPC;
  - shall be eligible to be a nominee for sole member of a OPC.
- No person shall be eligible to incorporate more than one OPC or become nominee in more than one such company.
- No minor shall become member or nominee of the OPC or can hold share with beneficial interest.

Q.3 Explain the meaning of Guarantee Company? State the similarities & dissimilarities, between a Guarantee Company & Company Limited by Share. [MTP May 2018], [MTP May 2019], [July 2021, 3 Marks]

Ans. "Company limited by guarantee" means a company having the liability of its members limited by the memorandum, to such amount as the members may respectively *undertake to contribute to the assets of the company in the event of its being wound up.*

These companies may or may not have a share capital. In the case of a guarantee company with a share capital, the members are required to purchase shares of fixed amount and also give a guarantee for a further sum in the event of winding up. *Generally, guarantee companies are formed for non-trading purposes. Such as promotion of commerce, art, science, sports etc., and do not aim for profit.* The Chambers of Commerce, charitable institutions, sport clubs, are generally organized as guarantee companies.

The **common features** between a 'guarantee company' and 'the company having share capital' are legal personality and limited liability. In the latter case, the member's liability is limited by the amount remaining unpaid on

the share, which each member holds. Both of them have to state in their memorandum that the members' liability is limited.

POINTS OF DISTINCTION	COMPANY LIMITED BY SHARES	COMPANY LIMITED BY GUARANTEE
Purpose:	Profit/non-profit both.	Generally not for profit.
Usefulness:	When initial funds are required to be raised to commence business.	Only where no working funds are needed or where these funds can be held from other sources like endowment, fees, charges, donations, etc.
Transfer of interest	May not be restricted.	Restricted & different than that of those limited by shares
Liability of members	Limited to amount unpaid on shares.	Limited to amount guaranteed.
Amount Called	Unpaid amount on shares may be called even before winding up.	Amount guaranteed can be called only on winding up. If company has a share capital, unpaid amount on shares can be called before winding up.
Share capital	Must have share capital	May or may not have share capital
To start	Raises initial funds from members	Does not raise initial funds from members, unless it has a share capital.

Q.4 "The Memorandum of Association is a charter of a company". Discuss. Also explain in brief the contents of Memorandum of Association.

[Nov. 2019, 6 Marks]

Ans. The Memorandum of Association of a company is regarded as its foundation which expresses the purpose of incorporation of the company and also spells out the conditions within the purview of which it is permitted to be formed & run its operations. The MOA not only defines the powers of the company proposed to be formed but in doing so also delimits/confines its powers. A company can enter only into those transactions & operations which are expressly permissible in the object clause of MOA or which are considered as ancillary or facilitative to the accomplishment of the expressly stated objects. Any transaction which falls beyond the scope of powers confessed by the MOA shall be regarded as *ultra vires* and therefore *void ab initio*.

The MOA can be truly regarded as constitution or charter of the company since it defines the scope of powers conferred on an artificial legal person *i.e.* a company. The MOA not only provides a clarity to the shareholders with respect to the purposes for which their contributed capital shall be utilised by the company but also provides the outsiders & dealing with the company, the certainty as to the nature & scope of their contractual relationships.

The following are the contents of MOA:

(*i*) *Name clause* - It states the name of the company. The name of a Public company must have 'Limited' as its last word, whereas the name of a private company must end with the word - 'Private Limited'.

(*ii*) *Registered office clause* - This clause must specify the name of the state in which the R.O of the company is proposed to be situated. The complete address of the company need not be mentioned in the MOA.

(*iii*) *Object clause* - The MOA of a company must state with clarity the purpose or the objects for which a company is proposed to be incorporated. It may also state such other objects which are necessary for accomplishment of main objects.

(*iv*) *Liability clause* - This clause expressly states the extent of liability of the members of the company. The liability of members shall be limited to the unpaid value of the share capital held by them, in case of a company limited by shares. Whereas in case of a company limited by guarantee the liability of the members shall be limited upto the amount guaranteed by them to be contributed on the event of winding up of the company.

(*v*) *Capital clause* - This clause in MOA of a company having share capital states the amount of share capital with which a company is proposed to be incorporated. The clause also states the number and type of shares in which the capital is divided into as well as the fixed amount or value of each share.

The number of shares that each subscriber to the MOA undertakes to subscribe must be indicated opposite his name. [at least 1 share]

Q.5 What are the significant points of section 8 company which are not applicable for other companies ? Briefly explain with reference to provisions of the Companies Act, 2013. [Nov. 2020, 6 Marks]

Ans. According to provisions of the Companies Act, 2013, section 8 deals with the formation of companies which are incorporated to promote the charitable objects of commerce, art, science, sports, education, research, social welfare, religion, charity, protection of environment etc. Such company intends to apply its profit in promoting its objects and prohibits the payment of any dividend to its members. Examples of section 8 companies are FICCI, ASSOCHAM, National Sports Club of India, etc.

Significant points of section 8 Companies which distinguish it from other companies:

- It is formed only for the promotion of commerce, art, science, religion, charity, protection environment, sports, etc.
- It uses its profits only for the promotion of the objective for which formed.
- It does not declare dividend to members.
- The requirement of minimum share capital does not apply.

- It operates under a special licence from Central Government, subject to certain conditions, and the license entitles it to avail certain privileges in comparison to other companies.
- It need not use the word Ltd./Pvt. Ltd. in its name and can adopt a names such as club, chambers of commerce etc.
- The licence can be revoked if the conditions subject to which it was issued are, contravened. On revocation, Central Government may direct it to – convert its status and change its name *i.e.* (add Ltd./Pvt. Ltd.) or may order it to wind-up or amalgamate with another company having similar objects, on such terms as the CG may deem appropriate.
- A section 8 company can call its general meeting by giving a clear 14 days' notice instead of 21 days.
- The requirement of minimum number of directors, independent directors etc. does not apply to a section 8 company.
- It need not constitute a Nomination Committee, Remuneration Committee and Shareholders' Relationship Committee.
- A partnership firm can be a member of section 8 Company.

Q.6 What do you mean by the term Capital? Describe its classification in the domain of Company Law. [Dec. 2021, 1 + 5 = 6 Marks]

Ans. CLASSIFICATION OF CAPITAL

The term 'Capital' has a variety of meanings. It means one thing to economists; another to accountants and still another to businessmen and lawyers. In relation to a company limited by shares, the word capital means share-capital, *i.e.*, the capital or figure in terms of so many rupees divided into shares of fixed amount. In other words, the contributions of persons to the common stock of the company form the capital of the company. The proportion of the capital to which each member is entitled, is his share. A share is not a sum of money; it is rather an interest measured by a sum of money and made up of various rights contained in the contract.

In the domain of Company Law, the term 'capital' is used in the following senses:

(*a*) **Nominal or authorised or registered capital:** This form of capital has been defined in section 2(*8*) of the Companies Act, 2013. "Authorised capital" or "Nominal capital" means such capital as is authorised by the memorandum of a company to be the maximum amount of share capital of the company. Thus, it is the sum stated in the memorandum as the capital of the company with which it is to be registered being the maximum amount which it is authorised to raise by issuing shares, and upon which it pays the stamp duty. It is usually fixed at the amount, which, it is estimated, the company will need, including the working capital and reserve capital, if any.

(*b*) **Issued capital:** Section 2(*50*) of the Companies Act, 2013 defines "issued capital" which means such capital as the company issues from time to

time for subscription. It is that part of authorised capital which is offered by the company for subscription and includes the shares allotted for consideration other than cash.

Schedule III to the Companies Act, 2013, makes it obligatory for a company to disclose its issued capital in the balance sheet.

(*c*) **Subscribed capital:** Section 2(*86*) of the Companies Act, 2013 defines "subscribed capital" as such part of the capital which is for the time being subscribed by the members of a company.

It is the nominal amount of shares taken up by the public. Where any notice, advertisement or other official communication or any business letter, bill head or letter paper of a company states the authorised capital, the subscribed and paid-up capital must also be stated in equally conspicuous characters. A default in this regard will make the company and every officer who is in default liable to pay penalty extending ₹ 10,000 and ₹ 5,000 respectively. [Section 60].

(*d*) **Called-up capital:** Section 2(*15*) of the Companies Act, 2013 defines "called-up capital" as such part of the capital, which has been called for payment. It is the total amount called-up on the shares issued.

(*e*) **Paid-up capital** is the total amount paid or credited as paid-up on shares issued. It is equal to called-up capital less calls in arrears.

SHORT QUESTIONS:

Q.7 When a company is registered, it is clothed with a legal personality. Explain. **[RTP May 2018]**

OR

What is the meaning of "Certificate of Incorporation" under the provisions of the Companies Act, 2013? What are the effects of registration of a company? **[MTP Nov. 2018]**

Ans. A company can be incorporated by complying with the formalities prescribed u/s 7 of the Companies Act, 2013. Application in the prescribed form must be made, alongwith the documents prescribed for this purpose and fees, to the Registrar within whose jurisdiction, the registered office of the company is proposed to be situated. The Registrar on being duly satisfied as to the compliance of all the requirements, relating to incorporation of a company, as prescribed under the Companies Act, 2013 and the rules made thereunder, shall register all the documents and information in the register and issue a certificate of incorporation in the prescribed form to the effect that the proposed company is incorporated under this Act. The certificate of incorporation shall also indicate the unique identity number allotted to the company *i.e.* the Corporate Identity Number, which shall be a distinct identity for the company.

When a company is registered and a certificate of incorporation is issued by the Registrar, following important consequences follow:—

1. The company becomes a **distinct legal entity**. Its life commences from the date mentioned in the certificate of incorporation.
2. It becomes a body corporate and it acquires a **perpetual succession.**
3. It is capable of suing and be sued in its corporate name.
4. Its property is not the property of the shareholders. The shareholders have a right to share in the profits of the company when realized and divided. Likewise any liability of the company is not the liability of individual shareholders.

From the date of incorporation mentioned in the certificate, the company becomes a legal person separate from the incorporators; and there comes into existence a binding contract between the company and its members as evidenced by the Memorandum and Articles of Association. It has perpetual existence until it is dissolved by liquidation or struck out of the register.

A legal personality emerges from the moment of registration of a company and from that moment the persons subscribing to the Memorandum of Association and other persons joining as members are regarded as a body corporate or a corporation in aggregate and the legal person begins to function as an entity. A company on registration acquires a separate existence and the law recognises it as a legal person separate and distinct from its members.

Q.8 Define a Small Company as defined under the Companies Act, 2013.

Ans. Small Company: Small company given under the section 2(*85*) of the Companies Act, 2013 which means a company, other than a public company—

(*i*) paid-up share capital of which does not exceed 2 crore rupees or such higher amount as may be prescribed which shall not be more than 10 crore rupees; and

(*ii*) turnover of which as per its last profit and loss account does not exceed 20 crore rupees or such higher amount as may be prescribed which shall not be more than 100 crore rupees:

Exceptions: This section shall not 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.

Q.9 Explain the concept of Dormant company as envisaged in the Companies Act, 2013. **[RTP May 2018]**

Ans. Where a company is formed and registered under this Act for a future project or to hold an asset or intellectual property and has no significant accounting transaction, such a company or an inactive company may make an

application to the Registrar in such manner as may be prescribed for obtaining the status of a dormant company.

"Inactive company" means a company which has not been carrying on any business or operation, or has not made any significant accounting transaction during the last two financial years, or has not filed financial statements and annual returns during the last two financial years.

"Significant accounting transaction" means any transaction other than—

(*i*) payment of fees by a company to the Registrar;

(*ii*) payments made by it to full the requirements of this Act or any other law;

(*iii*) allotment of shares to full the requirements of this Act; and

(*iv*) payments for maintenance of its office and records.

Q.10 Explain listed company and unlisted company as per the provisions of the Companies Act, 2013. [Dec. 2022, 2 Marks]

Ans.: Listed Company : As per the definition given in section 2(*52*) of the Companies Act, 2013, it is a company which has any of its securities listed on any recognized stock exchange:

Provided that such class of companies, which have listed or intend to list such class of securities, as may be prescribed in consultation with the Securities & Exchange Board, shall not be considered as listed companies.

Unlisted Company: Under the provisions of Companies Act, 2013 unlisted company means a company other than a listed company.

Q.11 Differentiate between the Memorandum of Association & Articles of Association.

Ans.

	MOA	AOA
Power	It is the charter and constitution of the company.	The articles are subordinate to memorandum. If there is conflict between the two, memorandum shall prevail.
Ultra vires	Acts done by a company beyond the scope of the memorandum are absolutely void (ineffective). They cannot be ratified even by unanimous vote of all the shareholders.	Articles of association govern the internal relationship between the company and its members. Acts done by the company beyond its Articles can be ratified by the shareholders.
Registration	Every company must have its own memorandum. It must be compulsorily filed for registration. It must be in the following forms: Model : A, B, C, D, E of Schedule I	Every company must have its own Articles. It must be compulsorily filed for registration. It must be in the following forms: Model : F, G, H, I, J of Schedule I

Alteration	MOA cannot be altered easily.	AOA can be altered if it is desired by 3/4th majority.
Nature	Memorandum of association contains the basic conditions on which the company is incorporated. It provides for name, situation objects, capital and liability of the company.	Articles of association are the rules governing the internal management of the company. It provides for rules and procedures for the conduct of its business.
Scope	It determines the objects, scope and extent of the activities of the company.	It governs the ways in which the objects of the company are to be carried out.

Q.12 State whether a non-profit organization can be registered as a company under the Companies Act, 2013. If so, what procedure does it have to adopt?

[RTP May 2018]

Ans. Formation of companies with charitable objects etc. (Section 8 company)

Section 8 of the Companies Act, 2013 deals with the formation of companies which are formed to—

- Promote the charitable objects of commerce, art, science, sports, education, research, social welfare, religion, charity, protection of environment etc.
- Such company intends to apply its profit in promoting its objects and
- Prohibiting the payment of any dividend to its members.

Examples of section 8 companies are FICCI, ASSOCHAM, National Sports Club of India, CII, etc.

Power of Central Government to issue the license—

(*i*) Section 8 allows the Central Government to register such person or association of persons as a company with limited liability without the addition of words 'Limited' or 'Private Limited' to its name, by issuing licence on such conditions as it deems fit.

(*ii*) The Registrar shall on application register such person or association of persons as a company under this section.

(*iii*) On registration the company shall enjoy same privileges and obligations as of a limited company.

Note: Central Government has delegated the power to grant license to the ROC.

Q.13 Examine with reasons whether the following statements are correct or incorrect with reasons:

(*i*) A private company must have a minimum of two members while a public company must have a minimum of seven members

[MTP May 2019]

(*ii*) Affixing of Common Seal on company's documents is compulsory. [MTP May 2018 & MTP May 2019]

(*iii*) A company being an artificial person cannot own property & cannot sue or be sued [RTP Nov. 2018]

Ans. (*i*) **Correct**. According to the provisions of section 3 of the Companies Act, 2013, which deals with the basic provisions for incorporation of a company, in case of public company a minimum of 7 persons is required to form a company to carry on the purpose as illustrated in the MOA of the company, by subscribing their name to the MOA. Similarly, a minimum of 2 persons is required to form a private company.

(*ii*) **Incorrect**. As per the Companies (Amendment) Act, 2015, the common seal has been made optional by omitting the words "and a common seal" from Section 9 of the Act, with a view to provide an alternative authorization for the purpose of creation of contract by a company. This amendment provides that in case a company does not have a common seal, the authentication shall be made by any key managerial personnel or an officer or employee of the company, duly authorised by the Board in this behalf.

(*iii*) **Incorrect** : A company is an artificial person and has separate legal entity independent of its members. As a consequence a company can enter into contracts in its own name, acquire and transfer/sell property in its own name and can also sue and be sued in its own name.

Q.14 What is meant by Doctrine of Constructive Notice?

Ans. Section 399 provides that the memorandum and articles when registered with Registrar of Companies **'become public documents'** and then they can be inspected by any one on payment of a nominal fee. Therefore, any person who contemplates entering into a contract with the company has the means of ascertaining the powers of the company and is thus, presumed to have read these documents and understood them in their true perspective. This is known as **"doctrine of constructive notice".**

Even if the party dealing with the company does not have actual notice of the contents of these documents it is presumed that he has an implied (constructive) notice of them. Consequently, if a person enters into a contract which is beyond the powers of the company, as defined in the memorandum, or outside the limit set on the authority of the directors as per the memorandum or articles, he cannot, as a general rule, acquire any rights under the contract against the company.

By constructive notice is meant

(*i*) Whether a person reads the documents or not, he is presumed to have knowledge of the contents of the documents. He is not only presumed to have read the documents but also understood them in their true perspective, and

(*ii*) Every person dealing with the company not only has the constructive notice of the memorandum and articles, but also of all the other related documents, such as Special Resolutions etc., which are required to be registered with the Registrar.

Thus, if a person enters into a contract which is beyond the powers of the company as defined in the memorandum, or outside the authority of directors as per memorandum or articles, he cannot acquire any rights under the contract against the company.

Q.15 Briefly explain the doctrine of 'ultra vires' under the Companies Act, 2013. What are the consequences of ultra vires acts of the company?

[RTP Nov. 2018, RTP May 2020]

OR

Explain the 'doctrine of *ultra vires* under the Companies Act, 2013. What are the consequences of '*ultra vires*' acts of the company?

[June 2022, 6 Marks]

Ans. The meaning of the term *ultra vires* is simply "beyond (their) powers". The legal phrase *"ultra vires"* is applicable only to acts done in excess of the legal powers of the doers. This presupposes that the powers in their nature are limited.

It is a fundamental rule of Company Law that the objects of a company as stated in its memorandum can be departed from only to the extent permitted by the Act, thus far and no further. In consequence, any act done or a contract made by the company which travels beyond the powers not only of the directors but also of the company is wholly void and inoperative in law and is therefore not binding on the company.

The impact of the doctrine of *ultra vires* is that a company can neither be sued on an *ultra vires* transaction, nor can it sue on it. Since the memorandum is a "public document", it is open to public inspection. Therefore, when one deals with a company one is deemed to know about the powers of the company. If in spite of this if a person enter into a transaction which is *ultra vires* the company, he cannot enforce it against the company.

Further an act which is *ultra vires* the company being void, cannot be ratified by the shareholders of the company. The leading case through which this doctrine was enunciated is that of ***Ashbury Railway Carriage and Iron Company Limited* v. *Riche* (1875).**

The following are the consequences of an *ultra vires* act of the company:—

(*i*) An act *ultra vires* the company is *null* and *void* and thus wholly inoperative. Neither the company can sue nor be sued against on such contract made for an *ultra vires* act.

(*ii*) An act which is *ultra vires* the company cannot be ratified even by the unanimous consent of all the shareholders.

(*iii*) An act which is *ultra vires* the company cannot become *'intra vires'* by reason of estoppel, acquiescence, lapse of time, delay or ratification.

(*iv*) The directors shall be held personally liable to the third parties who contracted for an *ultra vires* transaction on behalf of the company.

Q.16 What is meant by entrenchment of provisions in the Articles of Association?

Ans. The articles may contain provisions for entrenchment (to protect something) to the effect that specified provisions of the articles may be altered only if conditions or procedures as that are more restrictive than those applicable in the case of a special resolution, are met or complied with.

The provisions for entrenchment shall only be made either on formation of a company, or by an amendment in the articles agreed to by all the members of the company in the case of a private company and by a special resolution in the case of a public company.

Where the articles contain provisions for entrenchment, whether made on formation or by amendment, the company shall give notice to the Registrar of such provisions in such form and manner as may be prescribed.

Q.17 What do you mean by 'Companies with charitable purpose' (Section 8) under the companies Act, 2013? Mention the conditions of the issue & revocation of the license of such company by the Government.

[May 2019, 6 Marks]

Ans. "Companies with Charitable Objects" (Section 8) refers to the companies incorporated for a purpose other than earning profits. Such companies which carry on activities other than those of a commercial nature can be incorporated after obtaining a license u/s 8.

The Central Government issues a license for incorporation of a company under section 8, if it is duly satisfied that—

(*i*) the proposed company is being incorporated to promote the charitable objects of commerce, art, science, sports, education, research, social welfare, religion, charity, protection of environment etc.

(*ii*) such a company intends to apply its profits in promoting its objects only &

(*iii*) company prohibits the payment of any dividend to its members.

The Central Government may by order revoke the license of the company:—

(*i*) where the company contravenes any of the requirements of the conditions of section 8, subject to which the license is issued or

(*ii*) where the affairs of the company are conducted fraudulently, or

(*iii*) where the affairs of the company are conducted in a manner that is violative of the objects, or

(*iv*) in a manner prejudicial to public interest.

Before such revocation, the Central Government must give a notice of its intention to revoke the license to the company and must also award the company, a reasonable opportunity of being heard.

Q.18 Explain Doctrine of 'Indoor Management' under the Companies Act, 2013. Also state the circumstances where the outsider cannot claim relief on the ground of 'Indoor Management'. [Jan. 2021, 6 Marks]

Ans. Doctrine of Indoor Management:

Doctrine of Indoor Management also known as Turquand Rule, is an exception to constructive notice, which implies that if an act is authorized by the AOA or MOA, then the outsider is entitled to assume that all the detailed formalities for doing that act have been observed by the company and its officers.

Thus if an outsider who has complied with the requirements of constructive notice *i.e.* he has not only read the public documents and has knowledge of the powers of the company and the extent to which they have been delegated to the officers of the company, but also understood them in their true perspective, then he can assume that the internal affairs of the company have been actually conducted regularly in the manner prescribed in the documents.

This doctrine is based on business convenience and justice since it is not reasonably possible for the outsiders to have knowledge of the state of internal management of the company. Thus the doctrine gives protection to the outsiders against the effects of internal irregularities of the company by making the company liable.

Q.19 State the limitations of the Doctrine of Indoor Management under the Companies Act, 2013. [May 2018, 3 Marks], [RTP Nov. 2020]

Ans. The Doctrine of Indoor Management or Turquand Rule has limitations of its own. That is to say, it is inapplicable to the following cases, namely:

***a*. Actual or constructive knowledge of irregularity**

The rule does not protect any person when the person dealing with the company has notice, whether actual or constructive, of the irregularity. **[*Howard* vs. *Patent Ivory Manufacturing Co.*]**

***b*. Suspicion of Irregularity/Negligence**

The doctrine is not applicable in case of negligent persons. If an officer of the company acts in a manner, which would not ordinarily be within his powers, the person dealing with him must make proper inquiries and satisfy himself as to the officer's authority. If he fails to make enquiry, he cannot rely on the rule. Where the transaction is unusual or not in the ordinary course of business, it is the duty of the outsider to make the necessary enquiry.

The protection of the "Turquand Rule" is also not available where the circumstances surrounding the contract are suspicious and therefore invite inquiry. **[*Anand Bihari Lal* vs. *Dinshaw & Co.*]**

c. **Forgery**

The doctrine of indoor management applies only to irregularities which might otherwise affect a transaction but it cannot apply to forgery which must be regarded as nullity. Forgery may in circumstances exclude the 'Turquand Rule'. **[*Ruben* vs. *Great Fingall Consolidated*]**

Q.20 Explain the classification of the companies on the basis of control as per the Companies Act, 2013. [July 2021, 6 Marks]

Ans. According to provisions of the Companies Act, 2013, following is the classification of companies on the basis of control:-

(*i*) Holding and Subsidiary Companies - Holding and subsidiary companies are relative terms.

According to section 2(*46*), a Holding company in relation to one or more other companies means a company of which such other companies are Subsidiary companies.

According to section 2(*87*) a Subsidiary company in relation to any other company (that is the holding company) means a company in which that holding company -

- controls the composition of the Board of directors or
- exercises or controls more than 1/2 of the total voting power either at its own or together with one or more of its subsidiary companies:

Provided that such class or classes of holding companies as may be prescribed shall not have layers of subsidiaries beyond such number as may be prescribed.

For the purpose of this section —

- a company shall be deemed to be a subsidiary company of the holding company even if the control referred to in the above clauses is of another subsidiary company of the holding company.
- the composition of a company's board of directors shall be deemed to be controlled by another company if that other company by exercise of some power exercisable by it at its discretion can appoint or remove all or majority of the directors.
- the expression company includes any body-corporate.

(*ii*) Associate Company:- According to the provisions of section 2(*6*) of the Companies Act, 2013, an Associate Company in relation to another company means a company in which that other company has a significant influence but which is not a subsidiary company of the company having such influence and includes a joint venture company.

For the purpose of this definition:

- the expression 'significant influence' means control of at least 20% of the total voting power or control of or participation in the business decisions under an agreement.

- the expression 'joint venture' means a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement.

CASE STUDIES:

Q.21 The Articles of Association of XYZ Ltd. provides that Board of Directors has the authority to issue bonds provided such issue is authorised by the shareholders by a necessary resolution in the general meeting of the company. The company was in dire need of funds & therefore it issued the bonds to Mr. X without passing any such resolution in the general meeting. Can Mr. X recover the money from the company? Decide, referring to the relevant provisions of the Companies Act, 2013.
[RTP May 2018]

Ans. As per the provisions of the Doctrine of Indoor Management, if an act is authorised by the AOA/MOA, then the outsider dealing with the company, is entitled to assume that all the formalities concerned with the act in question, have been complied with by the company in a regular manner, provided he has knowledge of the formalities mentioned in the MOA/AOA. Thus if the outsider has knowledge of the contents of these public documents and has understood them in their true perspective, then doctrine offers protection to the outsider and allows him to enforce the said contract against the company.

The facts of the case are similar to the leading case, of *The Royal British Bank v. Turquand*, where the directors of RRB Ltd. issued a bond to Turquand. The AOA, empowered the directors to issue such bond under the authority of a proper resolution. In fact no such resolution was passed. Notwithstanding that, it was held that T could sue on the presumption of Doctrine of Indoor Management.

Thus it can be concluded applying the above provisions and the ruling of the leading case, that Mr. X can recover the money from the company, assuming that all the required formalities for passing the resolution has been duly complied.

Q.22 Krishna, an assessee, was a wealthy man earning huge income by way of dividend and interest. He formed three private companies and agreed with each to hold a block of investment as an agent for them. The dividend and interest income received by the companies was handed back to Krishna as a pretended loan. This way Krishna divided his income into three parts in a bid to reduce his tax liability. Decide for what purpose the three companies were established? Whether the legal personality of the three companies may be disregarded?
[MTP May 2018, MTP Nov. 2018, MTP May 2019]

Ans. A company on being incorporated acquires a separate legal existence. Its existence is distinct and separate from its members. This principle of separate legal entity may be referred to as the veil of incorporation. Generally the law does not disregard this 'corporate veil' and does not concern itself directly with the members or the directors of the company. However in certain exceptional cases the law shall disregard the corporate entity and pay regard to the realities behind the legal facade, in order to render justice. One of the circumstances where the corporate veil is lifted, is for protection of revenue of the Government. Thus where the corporate entity is being used as a means of evasion of taxes there the corporate veil shall be lifted.

In the given case, Krishna an assessee earning huge dividend and interest income, formed three private companies and agreed to hold the investments as an agent, and received back the dividend & interest income as a pretended loan, with the intention to reduce his taxation liability.

Thus it is evident that the three private companies have been incorporated to merely serve as a means for evading taxes by Krishna & the corporate veil shall be lifted and the separate entity shall be disregarded. The dividend and interest income shall be deemed to be that of Krishna and he shall be liable to pay tax on the same, as was held in the leading case of ***Sir Dinshaw Maneckjee Petit.***

Q.23 Ravi Private Limited has borrowed ₹ 5 crores from Mudra Finance Ltd. This debt is ultra vires to the company. Examine whether the company is liable to pay this debt? State the remedy if any available to Mudra Finance Ltd. [May 2018, 4 Marks]

Ans. A company cannot depart from the provisions contained in its M.O.A., however imperative may be the departure. It cannot enter into a contract that is beyond the power confessed on it by the M.O.A. If it does so, the contract shall be regarded as *ultra vires* and therefore *void ab initio*. The impact of an *ultra vires* transaction is that neither the company nor the third party has a right to sue on it. Since the memorandum is a public document by virtue of its being filed with the R.O.C., the parties who come to contract with the company, are deemed to have a knowledge of the contents of the M.O.A. If in spite of this the person enters into an *ultra vires* transaction, he cannot enforce the same against the company. Further money has been advanced to a company, in an *ultra vires* transaction, generally it cannot be recovered by the lender. However if the company has not yet expended the money then the company can be stopped from parting with the same by means of a suit for injunction and the lender shall be entitled to take back the same in specie.

In the given case Ravi Private Limited has borrowed ₹ 5 crore from Mudra Finance Ltd. which is *ultra vires*, which implies that Ravi Pvt. Ltd. has borrowed the amount beyond the limit prescribed in the M.O.A. of the company.

Applying the above stated effect of doctrine of *ultra vires*, it can be concluded that since the act of Ravi Pvt. Ltd. is *ultra vires* the company, the transaction shall be treated as *void ab initio*. However the lender *i.e.*, Mudra Finance Ltd.

shall be entitled to stop Ravi Pvt. Ltd. from parting with the money lent and take back the property in specie.

Q.24 ABC Pvt. Ltd., is a Private Company having five members only. All the members of the company were going by car to Mumbai in relation to some business. An accident took place and all of them died. Answer with reasons, under the Companies Act, 2013 whether existence of the company has also come to the end? [RTP Nov. 2018]

Ans. Company on its incorporation enjoys perpetual succession on account of its separate legal entity. The members may come and go but the company shall continue to be in existence for ever until the company is legally wound up. Further since the shares are transferable, in the event of death of the members, the shares shall be transmitted to their legal representatives. Thus the company, ABC Pvt. Ltd. shall continue to be in existence, inspite of the death of its members in the given case.

Q.25 The paid-up Share Capital of AVS Private Limited is ₹ 1 crore, consisting of 8 lacs Equity Shares of ₹ 10 each, fully paid-up and 2 lacs Cumulative Preference Shares of ₹ 10 each, fully paid-up. XYZ Private Limited and BCL Private Limited are holding 3 lacs Equity Shares and 1,50,000 Equity Shares respectively in AVS Private Limited. XYZ Private Limited and BCL Private Limited are the subsidiaries of TSR Private Limited. With reference to the provisions of the Companies Act, 2013, examine whether AVS Private Limited is a subsidiary of TSR Private Limited? Would your answer be different if TSR Private Limited has 8 out of total 10 directors on the Board of Directors of AVS Private Limited?

Ans. Section 2(87) defines "subsidiary company" in relation to any other company (that is to say 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 section—

(*i*) a company shall be deemed to be a subsidiary company of the holding company even if the control referred to in sub-clause (*i*) or sub-clause (*ii*) is of another subsidiary company of the holding company;

(*ii*) the composition of a company's Board of Directors shall be deemed to be controlled by another company if that other company by exercise of some power exercisable by it at its discretion can appoint or remove all or a majority of the directors.

Thus applying the above stated provisions, in both the above cases, AVS Pvt. Ltd. will be the subsidiary of TSR Pvt. Ltd. Total share capital of AVS Pvt. Ltd.

is of 8,00,000 shares out of which TSR Pvt. Ltd. is holding 4,50,000 shares through its subsidiaries.

Q.26 The Articles of a company required that all deeds etc. should be signed by the M.D., the Secretary and an Executive Director on behalf of the company. A deed of mortgage was signed by the Managing Director on behalf of the company in favour of Z. Can it be a valid deed?

Ans. Hint: Doctrine of constructive Notice; The Articles require the deed to be signed by 3 persons. Z should have consulted the Articles of Association of the company to ascertain the authority of signing the deed. Even if, the M.D. has signed it in good faith, the deed is still not valid. Z can't claim on the basis of the deed. The concept is that since the Articles is a public document, on being filed with the ROC, Z is presumed to have known its provisions. This principle was laid in *Kotla Venkateswami* v. *Ramamurthy* AIR 1934 Mad 579.

Q.27 The Object Clause of Memorandum of Association of ABC Pvt. Ltd. Authorized the company to carry on the business of trading in Fruits and Vegetables. The Directors of the company in recently concluded Board Meeting decided and accordingly, the company ordered for fish for the purpose oftrading. FSH Limited supplied fish to ABC Pvt. Ltd. Worth ₹ 36 lakhs. The members of the company convened an extraordinary general meeting and negated the proposal of the Board of Directors on the ground of *ultra vires* acts. FSH Limited being aggrieved of the said decision of ABC Pvt. Ltd. seeks your advice. Advice them.
[MTP Nov. 2018]

Ans. Hint:- Doctrine of *ultra vires*; Company being an artificial person can enter into those contracts as are warranted by terms of the object clause of its MOA. A company can depart from the objects stated in MOA only to the extent permitted by the Act, thus far and no further. Thus any act done or any contract made by the company which travels beyond the powers not only of the directors but also of the company is wholly void inoperative and is therefore not binding on the company.

In the given case the object clause of MOA of ABC Pvt. Ltd. authorizes to carry on the business of trading in fruits & vegetables only, whereas the company enters into a contract with FSH Ltd. for purchase of fish worth ₹ 36 lakhs.

Thus the contract is *ultra vires* the company and shall not be binding on the company. Further ratification of *ultra vires* transactions cannot be done even by the whole body of shareholders. Thus FSH Ltd. has no remedy against the company. It can hold the directors of ABC Pvt. Ltd. personally liable.

Q.28 FAREB Limited was incorporated by acquisition of Fareb & Co., a partnership firm, which was earlier involved in many illegal activities. The promoters furnished some false information and also suppressed some material facts at the time of incorporation of the company. Some

members of the public (not being directors or promoters of the company) approached the National Company Law Tribunal (NCLT) against the incorporation status of FAREB Limited. NCLT is about to pass the order by directing that the liability of the members of the company shall be unlimited.

Given the above, advice on whether the above order will be legal and mention the precaution to be taken by NCLT before passing order in respect of the above as per the provisions of the Companies Act, 2013. [MTP Nov. 2018]

Ans. According to the provisions of section 7(7) of the Companies Act, 2013, where a company has been got incorporated by furnishing false or incorrect information or representation or by suppressing any material fact or information in any of the documents or declaration filed or made for incorporating such company or by any fraudulent action, the Tribunal may, on an application made to it, on being satisfied that the situation so warrants,—

(*a*) pass such orders, as it may think fit, for regulation of the management of the company including changes, if any, in its memorandum and articles, in public interest or in the interest of the company and its members and creditors; or

(*b*) direct that liability of the members shall be unlimited; or

(*c*) direct removal of the name of the company from the register of companies; or

(*d*) pass an order for the winding up of the company; or

(*e*) pass such other orders as it may deem fit:

Provided that before making any order,—

- the company shall be given a reasonable opportunity of being heard in the matter; and
- the Tribunal shall take into consideration the transactions entered into by the company, including the obligations, if any, contracted or payment of any liability.

Further where it is proved that a company has been incorporated as aforesaid, then the promoters, the persons named as the first directors and the persons making declaration at the time of incorporation of the company shall each be liable for action for fraud under section 447.

In the given case, the decision of NCLT to direct that the liability of the members of FAREB Ltd. shall be unlimited is legally valid as per the above stated provisions. However before passing any such direction NCLT shall grant FAREB Ltd. an, opportunity of being heard and shall take into consideration the transactions entered into by company, including the obligations if any contracted or payment or any liability.

Q.29 A company registered under section 8 of the Companies Act, 2013, earned huge profits during the financial year ended on 31st March, 2018 due to some favourable policies declared by the Government of India

and implemented by the company. Considering the development, some members of the company wanted the company to distribute dividends to the members of the company. They approached you to advise them about the maximum amount of dividend that can be declared by the company as per the provisions of the Companies Act, 2013. Examine the relevant provisions of the Companies Act, 2013 and advise the members accordingly. [Nov. 2018, 4 Marks], [MTP Nov. 2019]

Ans. According to provisions of section 8 of the Companies Act, 2013, a company can be incorporated for not-for-profit purpose under a license from Central Government provided the following conditions are complied :—

(*i*) The company is formed to promote the charitable objects of commerce, art, science, sports, education, research, social welfare, religion, charity protection of environment etc.

(*ii*) Such a company intends to apply its profits/surplus in the promotion of its objects and

(*iii*) The payment of dividend to its members is prohibited.

In the given case the member of a section 8 company are desirous that the company should distribute dividends out of the huge profits earned by the company, among its members.

Thus applying the above stated provisions it is evident that distribution of dividend is prohibited and therefore the claim of the members is not tenable.

Q.30 Mr. X had purchased some goods from M/s. ABC Limited on credit. A credit period of one month was allowed to Mr. X. Before the due date Mr. X went to the company and wanted to repay the amount due from him. He found only Mr. Z there, who was the factory supervisor of the company, Mr. Z told Mr. X that the accountant and the cashier were on leave, he is in-charge of receiving money and he may pay the amount to him. Mr. Z issued a money receipt under his signature. After two months M/s. ABC Limited issued a notice to Mr. X for non-payment of the dues within the stipulated period. Mr. X informed the company that he had already cleared the dues and he is no more responsible for the same. He also contended that Mr. Z is an employee of the company to whom he had made the payment and being an outsider, he trusted the words of Mr. Z as duty distribution is a job of the internal management of the company.

Analyse the situation and decide whether Mr. X is free from his liability.

[Nov. 2018, 3 Marks] [MTP May 2019], [MTP May 2021]

Ans. The Doctrine of Indoor Management is an exception to the Doctrine of Constructive Notice. An outsider who has read the public documents (MOA & AOA) containing the powers of the company and the extent to which they have been delegated to its officers and understood them in their true perspective, can assume that the internal operations and management of the company have been performed regularly, in respect of the contract that he is desirous

of entering into with the company. However there are certain limitations of this doctrine.

One of the exceptions to the Doctrine of Indoor management is knowledge/ suspicion of irregularity. The protection under the doctrine does not extend to those persons who have behaved negligently. Thus when the circumstances are such which invite enquiry & for example when an officer of the company is purporting to act in a matter, which is apparently outside the usual scope of his authority, then the outsides is under a duty to make the necessary enquiry. If the outsider fails to make inquiry as such then he cannot seek protection under the Doctrine of Indoor Management and the company shall not be bound by the transaction. This was also held in the case of ***Anand Behari Lal*** v. ***Dinshaw & Co.***

In the given case Mr. X makes the payment to Mr. Z the factory supervisor. The act of receiving money on behalf of the company falls beyond the apparent authority of a factory supervisor. The nature of transaction was such which required Mr. X to enquire as to Mr. Z's authority.

Thus applying the above stated provisions it can be concluded that Mr. X is not free from his liability towards the company as he failed to enquire about Mr. Z's authority despite the suspicious circumstances.

Q.31 Sound Syndicate Ltd. a public company, its articles of association empowers the managing agents to borrow both short and long-term loans on behalf of the company. Mr. Liddle the director of the company, approached Easy finance Ltd., a non-banking finance company for a loan of Rs. 25,00,000 in name of the company. The lender agreed and provided the said loan. Later on Sound Syndicate Ltd. refused to repay the money borrowed on the pretext that no resolution authorizing such loan have been actually passed by the company and the lender should have enquired about the same prior to providing such loan. Hence the company is not liable to pay such loan. Analyse the above situation in terms of the provisions of Doctrine of Indoor Management under the Companies Act, 2013 and examine whether the contention of Sound Syndicate Ltd. is correct or not? [May 2019, 4 Marks]

Ans. According to the provisions of Doctrine of Indoor Management, an outsider while entering into contracts with a company is entitled to assume, due & regular compliance of all the formalities & internal proceedings required on the part of the company for the purpose of the contract, provided the outside has the knowledge, of the scope of authority of the company as contained in the MoA and also of the extent to which the authority has been delegated to the officials of the company. Thus an outsider can plead protection against the internal irregularities in the operations of the company & hold the company liable under the contract, only if he has the knowledge of MoA as well as the AoA and has understood their terms in their true perspective. In case the third

party (outsider) has no knowledge of MoA & AoA then it cannot seek remedy under Doctrine of Indoor Management.

In the given case sound Syndicate Ltd. contracts with Easy Finance Ltd. to borrow a loan of Rs. 25,00,000. The AoA of sound Syndicate Ltd. empower its managing agents (*i.e.* directors) to borrow loans on its behalf.

Thus applying the above stated provisions to the given case it can be concluded that if Easy Finance Ltd. had the knowledge of the AoA of Sound Syndicate Ltd. & was aware of the power of its directors to borrow loans on behalf of the company, then the fact, that no resolution authorising the directors was actually passed, shall be of no consequence & Easy Finance Ltd. can hold the company liable for the loan.

Passing of resolution authorising the loan is a matter of internal management of the company which will be presumed to have been regularly performed, provided Easy Finance Ltd. has the knowledge of the AoA of Sound Syndicate Ltd. Thus the contention of Sound Syndicate Ltd. is not correct.

Q.32 The Memorandum and Articles of Association of a company were delivered to the Registrar of Companies for registration on January 6, 2018. On January 8th, 2018, the Registrar issued the certificate of incorporation but dated it January 6th, 2018. On that very day (January 6th, 2018) the company made allotment of its shares. The allotment was challenged that it was made before the actual issue of the certificate of incorporation. How would you decide and why?

Ans. Hint: According to the provisions of the Companies Act, 2013, a company comes into existence the moment it is incorporated and a certificate of incorporation is issued. The company acquires a separate legal entity, from the date mentioned in the certificate and becomes competent to enter into contract in its own name, purchase assets, incur liabilities in its own name and sue and be sued in its own name.

Thus in the given case the company has acquired a separate legal entity form the date of its incorporation as appearing in the certificate, *i.e.* 6th January, 2018. Therefore the contract for allotment of shares made by the company is valid.

Q.33 Popular Products Ltd. is a company incorporated in India, having a total Share Capital of ₹ 20 Crores. The Share capital comprises of 12 Lakhs equity shares of ₹ 100 each and 8 Lakhs Preference Shares of ₹ 100 each. Delight Products Ltd. and Happy products Ltd. hold 2,50,000 and 3,50,000 shares respectively in Popular Products Ltd. Another company Cheerful products Ltd. holds 2,50,000 shares in Popular Products Ltd. Jovial Ltd., is the holding company for all above three companies namely Delight Products Ltd.; Happy products Ltd; Cheerful products Ltd. Can Jovial Ltd., be termed as subsidiary company of Popular Products Ltd., if it Controls composition of directors of Popular Products Ltd. State the related provision in the favour of your answer. [May 2019, 3 Marks]

Ans. According to the provisions of section 2(46) of the Companies Act, 2013, a company is a holding company in relation to one or more other companies, means a company of which such companies are subsidiary companies.

Further section 2(*87*) defines subsidiary company in relation to any other company (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 share capital either at its own or together with one or more of its subsidiary companies.

A company shall be deemed to be a subsidiary company of the holding company even if the control referred to in sub-clauses (*i*) & (*ii*) is of another subsidiary company of the holding company.

In the given case subsidiaries of Jovial Ltd. - Delight Products Ltd.; Happy Products Ltd. & Cheerful Products Ltd. hold 2,50,000; 3,50,000 & 2,50,000 shares respectively in Popular Ltd. The total shareholding of these subsidiaries amounts to 8,50,000 shares which is more than half of the total share capital of Popular Ltd. of 12,00,000 No. of shares. Thus Jovial Ltd. is controlling more than half of share capital of Popular Ltd. through its subsidiaries.

Further if Jovial Ltd. is in a position to exercise control over the composition of Board of Directors of Popular Ltd. then also Jovial Ltd. shall be regarded as the holding company of Popular Ltd.

Thus it can be concluded that Jovial Ltd. is not the subsidiary, but is rather the holding company of Popular Ltd.

Q.34 Mr. Anil formed a One Person Company (OPC) on 16th April, 2018 for manufacturing electric cars. The turnover of the OPC for the financial year ended 31st March, 2019 was about ₹ 2.25 Crores. His friend Sunil wanted to invest in his OPC, so they decided to convert it voluntarily into a private limited company. Can Anil do so?

[Nov. 2019, 4 Marks] [Dec. 2022, 4 Marks]

Ans. According to the provisions of the Companies Act, 2013, a one person Company cannot voluntarily convert itself into any kind of company unless 2 years have expired from the date of incorporation except where the paid-up capital is increased beyond ₹ 50,00,000 or its average annual turnover during the relevant period exceeds ₹ 2 crores.

In the given case Mr. Anil incorporated OPC on 16th April, 2018. The turnover of the company was ₹ 2.25 crores for the financial year ended 31st March, 2019.

Thus applying the above stated provisions it can be concluded that the OPC can be validly converted into a private company even though 2 years have not expired from incorporation since the turnover for 1 year itself exceeds ₹ 2 crores.

Students, please note, that the above question has been wrongly asked since the provisions regarding restriction on conversion of OPC, on which the said question has been based, has already been deleted as per the

amendment w.e.f. 1.04.2021. Thus now OPC can be converted into any other type of company at any time.

Q.35 ABC Limited has allotted equity shares with voting rights to XYZ Limited worth ₹ 15 Crores and issued Non-Convertible Debentures worth ₹ 40 Crores during the Financial Year 2019-20. After that total Paid-up Equity Share Capital of the company is ₹ 100 Crores and Non-Convertible Debentures Stand at ₹ 120 Crores.

Define the Meaning of Associate Company and comment on whether ABC Limited and XYZ Limited would be called Associate Company as per the provisions of the Companies Act, 2013 ? [Nov. 2020, 4 Marks]

Ans. According to the provisions of section 2(*6*) of the Companies Act, 2013 an Associate Company in relation to another company means a company in which that other company has a significant influence, but which is not a subsidiary company of the company having such influence and includes a joint venture company. For the purpose of this clause: the expression "significant influence" means control of at least 20% of total voting power or control of or participation in business decisions under an agreement.

In the given case XYZ Ltd. is holding Equity shares with voting rights worth ₹ 15 crores and Non-convertible debentures worth ₹ 40 crores in ABC Ltd. Further in computing "significant influence" as aforesaid, the holding in respect of Non-convertible debentures shall not be considered since they do not carry voting rights.

It is therefore evident that XYZ Ltd. holds voting rights amounting to only 15% of the total voting power (15/100 × 100) of ABC Ltd. which is less than 20% of total voting power required minimally to be regarded as significant influence. Thus it can be concluded that ABC Ltd. is not the Associate Company of XYZ Ltd.

Q.36 Mike Limited company is incorporated in India and having Liaison office at Singapore. Explain in detail meaning of Foreign Company and analyse, on whether Mike Limited would be called as Foreign Company as it established a Liaison office at Singapore as per the provisions of the Companies Act, 2013 ? [Nov. 2020, 3 Marks]

Ans. According to section 2(*42*) of the Companies Act, 2013 a foreign company means any company or body corporate incorporated outside India which:

(*i*) has a place of business in India whether by itself or through an agent, physically or through electronic mode, and

(*ii*) conducts any business activity in India in any other manner.

In the given case Mike Limited is incorporated in India & having liaison office at Singapore.

Thus applying the above stated provisions, it is evident that since Mike Limited is incorporated in India therefore it would not be called as foreign company under Companies Act, 2013.

Q.37 ABC Limited was registered as a public company. There were 245 members in the company. Their details are as follows :

Directors and their relatives	**190**
Employees	**15**
Ex-employees (shares were allotted when they were employees)	**20**
Others	**20**

(Including 10 joint holders holding shares jointly in the name of father and son)

The Board of directors of the company propose to convert it into a private company. Advice whether reduction in the number of members is necessary for conversion. [Jan. 2021, 4 Marks]

Ans. According to the provisions of section 2(*68*) of the Companies Act, 2013, Private Company means a company having minimum paid-up share capital as may be prescribed and which by its articles :

(*i*) restricts the right to transfer its shares;

(*ii*) except in case of OPC, limits the number of members to 200:

Provided that where two or more persons hold one or more shares in a company jointly, they shall, for the purposes of this clause, be treated as a single member:

Provided further that—

- persons who are in the employment of the company; and
- persons, who having been formerly in the employment of the company, were members of the company while in that employment and have continued to be the members after the employment ceased, shall not be included in the number of members; and

(*iii*) prohibits any invitation to the public to subscribe for any securities of the company.

In the given case ABC Ltd. has 245 members of which 10 were joint shareholders holding shares in the name of father and son, 15 were current employees and 20 were ex-employees who became members of the company at the time of their employment with the company.

Thus applying the above stated provisions it is evident that ABC Ltd. actually has a total of 205 members since 10 joint shareholders holding shares in the name of father and son shall be counted as single member *i.e.* as 5 members, and 15 current employees and 20 ex-employees shall not be counted in computing the number of members.

Therefore it can be concluded that in the event of conversion of ABC Ltd. into a private company as proposed by the Board of Directors, the number of members would be required to be reduced from the current 205 to 200 so as to ensure compliance with the requirement of section 2(*68*) in respect of the maximum number of members in a Private Company.

Q.38 SK Infrastructure Limited has a paid-up share capital divided into 3,60,000 equity shares of INR 100 each. 2,00,000 equity shares of the company are held by Central Government and 1,20,000 equity shares are held by Government of Maharashtra. Explain with reference to relevant provisions of the Companies Act, 2013, whether SK Infrastructure Limited can be treated as Government Company. [Nov. 2020, 3 Marks]

Ans. According to the provisions of section 2(*45*) of the the Companies Act, 2013, a Government company means a company in which not less than 51% of the paid-up share capital is held by the Central Government, or by a State Government or partly by Central and partly by one or more State Governments and the section includes a company which is a subsidiary of such a Government company.

In the given case 2,00,000 equity shares of SK Infrastructure Ltd. are held by the Central Government and 1,20,000 equity shares are held by Government of Maharashtra. This amounts to more than 51% of the total paid-up share capital (6,00,000) in SK Infrastructure Ltd. Thus applying the above provisions to the given case it is evident that SK Infrastructure Ltd. is a Government company since more than 51% of paid-up share capital is held partly by the Central Government and partly by the State Government of Maharashtra.

Q.39 Alfa school started imparting education on 1.4.2010, with the sole objective of providing education to children of weaker society either free of cost or at a very nominal fee depending upon the financial condition of their parents. However, on 30th March 2018, it came to the knowledge of the Central Government that the said school was operating by violating the objects of its objective clause due to which it was granted the status of a section 8 company under the Companies Act, 2013. Describe what power can be exercised by the Central Government against the Alfa School, in such a case ? [MTP May 2021]

Ans. According to the provisions of section 8 of the Companies Act, 2013, a company which carries on activities other than those of a commercial nature, can be incorporated after obtaining license u/s 8 provided the said company meet all the requirements under section 8. Further the Central Government may by order revoke the license granted where the company contravenes any of the requirements of section 8, subject to which license is issued or where the affairs of the company are being conducted in a manner that is violative of the objects. On the revocation of license, the registrar shall add the words 'Limited' or 'Private Limited', as the case may be, to the name of the company.

Where a license 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 be amalgamated with another company registered under this section & having similar objects. Further when an order for amalgamation is passed, then the Central Government may provide for such amalgamation to form a single company, with such constitution, properties, privileges, rights and such liabilities & obligations, as it may specify.

Thus in the given case, since Alfa school has been conducting activities in violation of its object clause, its license can be revoked and the Central Government can resort to any of the above courses of actions. However, before passing any order the Central Government shall give Alfa school, a reasonable opportunity of being heard.

Q.40 Y incorporated a "One Person Company (OPC)" making his sister Z as nominee. Z is leaving India permanently due to her marriage abroad.

Due to this fact, she is withdrawing her consent of nomination in the said OPC. Taking into considerations the provisions of the Companies Act, 2013 answer the questions given below :

(*i*) Is it mandatory for Z to withdraw her nomination in the said OPC, if she is leaving India permanently ?

(*ii*) Can Z continue her nomination in the said OPC, if she maintained the status of Resident of India after her marriage ?

[July 2021, 4 Marks]

Ans. According to the provisions of section 3 of the Companies Act, 2013, only a natural person who is an Indian citizen whether resident in India or otherwise and has stayed in India for a period of not less than 120 days during the immediately preceding financial year, shall be eligible to incorporate OPC & shall be eligible to be a nominee for the sole member of OPC.

In the given case Y who has incorporated an OPC, has made his sister Z as a nominee, who is now leaving India permanently due to her marriage abroad & is withdrawing her consent due to this reason:

(*i*) In the light of the above stated provision it can be concluded that Z is rightfully withdrawing her consent as she is leaving India permanently and will not be regarded as resident in India since she will not be meeting the criteria of residing in India of 120 days.

(*ii*) However if Z can maintain her residential status of 'Resident of India' after her marriage, residing in India for not less than 120 days in the preceding financial year, then she need not withdraw her nomination, since she will then qualify the eligibility requirement as prescribed under section 3.

Q.41 AK Private Limited has borrowed ₹ 36 crores from BK Finance Limited. However, as per memorandum of AK Private Limited the maximum borrowing power of the company is ₹ 30 crores. Examine, whether AK Private Limited is liable to pay this debt? State the remedy, if any available to BK Finance Limited. [Dec. 2021, 4 Marks]

Ans. Hint: Contracts which are *ultra vires* and fall beyond the scope of MOA are *void ab initio* and not binding on the company.

Thus in the given case, the loan is *ultra vires* AK Private Ltd. and the company is not bound by it. However as a remedy BK Private Ltd. can file a suit against the directors of the company and hold them personally liable. Further BK Private Ltd. can file a suit for injunction and prevent, AK Private Ltd. from parting with the money borrowed.

Q.42 BC Private Limited and its subsidiary KL Private Limited are holding 90,000 and 70,000 shares respectively in PQ Private Limited. The paid-up share capital of PQ Private Limited is ₹ 30 Lakhs (3 Lakhs equity shares of ₹ 10 each fully paid). Analyse with reference to provisions of the Companies Act, 2013 whether PQ Private Limited is a subsidiary of BC Private Limited. What would be your answer if KL Private Limited is holding 1,60,000 shares in PQ Private Limited and no shares are held by BC Private Limited in PQ Private Limited? [Dec. 2021, 3 Marks]

Ans. According to the provisions of section 2(*87*) of the Companies Act, 2013, a subsidiary company in relation to any other company (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.

Further a company shall be deemed to be a subsidiary company of the holding company even if the control referred to in sub-clauses (*i*) & (*ii*) is of another subsidiary company of the holding company.

In the given case BC Private Ltd. & it's subsidiary- KL Private Ltd. are holding 90,000 & 70,000 shares respectively in PQ Private Ltd., which amounts to 1,60,000 shares, which is more than half of the equity share capital of PQ Private Ltd. of 3 lakh shares.

Thus it is evident that BC Private Ltd. along with its subsidiary, KL Private Ltd. holds more than half of the total voting power of PQ Private Ltd. Therefore, PQ Private Ltd. will be regarded as the subsidiary company of BC Private Ltd.

If in the given case KL Private Ltd. holds 1,60,000 shares in PQ Private Ltd., then also PQ Private Ltd. will be deemed as a subsidiary company of BC Private Ltd. and the answer will remain unchanged.

Q.43 The Articles of Association of Aarna Limited empowers its managing agents to borrow loans on behalf of the company. Ms. Anika, the director of the company, borrowed ₹ 18 Lakhs in name of the company from Quick Finance Limited, a non-banking finance company. Later on, Aarna Limited refused to repay the money borrowed on the pretext that no resolution authorizing such loan have been actually passed by the company and therefore the company is not liable to pay such loan.

Decide whether the contention of Aarna Limited is correct in accordance with the provisions of the Companies Act, 2013? [June 2022, 4 Marks]

Ans. Hint: Doctrine of Indoor Management offers protection to outsiders against internal irregularities in the operations of Company and holds the Company liable.

Passing of a resolution authorising the loan is a matter of internal management of the company which will be presumed to have been regularly passed, provided Quick Finance Limited has knowledge of the AOA of Arna Limited. Thus, the contention of Arna Limited is not correct.

Q.44 Mr. R is an Indian citizen, and his stay in India during the immediately preceding financial year, is for 130 days. He appoints Mr. S, a foreign citizen, as his nominee, who has stayed in India for 125 days during the immediately preceding financial year. Is Mr. R eligible to be incorporated as a One-Person Company (OPC)? If yes, can he give the name of Mr. S in the memorandum of Association as his nominee? Justify your answers with relevant provisions of the Companies Act, 2013. [June 2022, 3 Marks]

Ans. According to the provisions of the Companies Act, 2013 relating to OPC, only a natural person who is an Indian Citizen, whether resident in India (*i.e.* who has stayed in India for a period of not less than 120 days during the immediately preceding financial year) or otherwise shall be eligible to incorporate a OPC and shall be eligible to be a nominee for the sole member of OPC.

In the given case Mr. R is an Indian Citizen who has stayed in India for 130 days and Mr. S is a foreign citizen who has stayed in India for 125 days during the immediately preceding financial year.

Thus applying the above stated provisions it is evident that Mr. R is eligible to incorporate OPC since he is a natural person, Indian citizen and resident in India. However, he cannot name Mr. S as his nominee in the MOA of OPC since he is a foreign citizen and therefore not eligible to be a nominee of OPC.

Q.45 Mr. R, a manufacturer of toys approached MNO Private Limited for supply of raw material worth ₹ 1,50,000. Mr. R was offered a credit period of one month. Mr. R went to the company prior to the due date and met Mr. C, an employee at the billing counter, who convinced the former that the payment can be made to him as the billing cashier is on leave.

Mr. R paid the money and was issued a signed and sealed receipt by Mr. C. After the lapse of due date, Mr. R received a recovery notice from the company for the payment of ₹ 1,50,000.

Mr. R informed the company that he has already paid the above amount and being an outsider had genuine reasons to trust Mr. C, who claimed to be an employee and had issued him a receipt.

The Company filed a suit against Mr. R for non-payment of dues. Discuss the fate of the suit and the liability of Mr. R towards company as on current date in consonance with the provision of the Companies Act, 2013? Would your answer be different if a receipt under the company seal was not issued by Mr. C after receiving payment? [Dec. 2022, 4 Marks]

Ans. According to the provisions of Company Law, if an outsider has complied with the requirements of constructive notice, then he can assume that the internal affairs of the company have been actually conducted regularly in the manner prescribed in the documents. This is the Doctrine of Indoor Management which operates as an exception to Constructive Notice and gives protection to the outsiders against the effects of the internal irregularities of the company.

However the said Doctrine has certain limitations and is inapplicable in certain cases, one of them being the instance where an outsider behaves negligently and despite suspicion of irregularity fails to enquire. Thus if an officer/employee of the company acts in a manner which would not ordinarily be within his powers, the person dealing with him must make proper inquiries and satisfy himself as to the officer's/employee's authority. If he fails to make enquiry, he cannot rely on the rule, nor can he seek protection under doctrine of Indoor management. Where the transaction is unusual or not in the ordinary course of business, it is the duty of the outsider to make the necessary enquiry, as was held in the leading case of ***Anand Bihari Lal vs. Dinshaw & Co.***

In the given case, Mr. R contracted with MNO Pvt. Ltd. for purchase of raw material worth ₹1,50,000. Later he went to pay the amount to company and met Mr. C an employee at the billing counter who convinced the former that the payment could be made to him as the billing cashier was on leave. Mr. R paid the money to Mr. C and received a receipt for the same. Later the company sent a recovery notice to Mr. R, demanding the payment.

Applying the above stated provisions it is evident that Mr. R failed to enquire into the authority of Mr. C, a common employee, to receive the payment in place of the billing cashier. Mr. R failed to enquire even when the circumstances were suspicious as an ordinary employee claimed to be authorized to receive payments on behalf of the company which was unusual. He behaved negligently and shall therefore not be entitled to seek protection under the Doctrine of Indoor Management. Thus Mr. R shall be held liable to make payment to the company.

No, the answer would not be any different even if a receipt under the Company seal was not issued by Mr. C to Mr. R.

Q.46 Mike LLC incorporated in Singapore having an office in Pune, India. Analyse whether Mike LLC would be called as a foreign company as per the provisions of the Companies Act, 2013? Also explain the meaning of foreign company. [Dec. 2022, 3 Marks]

Ans. According to the provisions of the Companies Act, 2013, a Foreign Company means any company or body corporate incorporated outside India which –

(*i*) has a place of business in India, whether by itself or through an agent, physically or through electronic mode; and

(*ii*) conducts any business activity in India in any other manner.

In the given case, Mike LLC is incorporated in Singapore and has an office in Pune, India.

Thus applying the above stated provisions, it is evident that Mike LLC shall be regarded as a Foreign Company under the provisions of the Companies Act, 2013.

Q. 47 ABC Limited has allotted equity shares with voting rights to XYZ Limited worth ₹ 15 crores and convertible preference shares worth ₹ 10 crores during the financial year 2022-23. After that the total share capital of the company is ₹ 100 crores.

Comment on whether XYZ Limited would be called an Associate Company as per the provisions of the Companies Act, 2013? Also define an Associate Company. [June 2023, 4 Marks]

Ans. According to the provisions of section 2(*6*) of the Companies Act, 2013, an Associate company, in relation to another company means a company in which that other company has a significant influence but which is not a subsidiary company of the company having such an influence and includes a joint venture company. Further for the purpose of this clause:

- the expression "significant influence" means control of at least twenty per cent of total voting power, or control of or participation in business decisions under an agreement.
- the expression "joint venture" means a joint arrangement whereby the parties that have joint control of the arrangements have the rights to the net assets of the arrangement.

In the given case ABC Ltd. has allotted equity shares with voting rights worth 15 crores and convertible preference shares worth 10 crores to XYZ Ltd. and the total share capital of ABC Ltd. including these shares is 100 crores.

Thus applying the above stated provisions to the given case it is evident that XYZ holds only 10% of the total voting rights in ABC Ltd. If the total voting rights held by XYZ Ltd. in ABC Ltd., would have been at least 20%, then ABC Ltd. would have been regarded as the Associate Company of XYZ Ltd. Therefore XYZ Ltd. is not an associate company of ABC Ltd.

Q.48 ABC Private Limited is a registered company under the Companies Act, 2013 with paid up capital of ₹ 35 lakhs and turnover of ₹ 2.5 crores. Whether the ABC Private Limited can avail the status of a Small Company in accordance with the provisions of the Companies Act, 2013? Also discuss the meaning of a Small Company. [June 2023, 3 Marks]

Ans. According to the provisions of section 2(*85*) of the Companies Act, 2013, a Small company, means a company other than public company -

(*i*) the paid up capital of which does not exceed 4 crore rupees or such higher amount as may be prescribed which shall not be more than 10 crore rupees and;

(*ii*) the turnover of which as per its last profit and loss statement does not exceed 40 crores or such higher amount as may be prescribed which shall not be more than 100 crore rupees.

In the given case, ABC Private limited, has a paid up capital of ₹ 35 lakh and a turnover of ₹ 2.5 crores. Thus applying the above stated provisions it is evident that, ABC Private limited can validly avail the status of a Small Company.