

SCANNER FOR CA FOUNDATION MAY' 19



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This scanner contains all the questions of


- RTP (May' 18, Nov' 18, May' 19, Nov' 19, May' 20, Nov' 20, May' 21))
- RTP (May' 18 – May' 21)
- Question papers (May' 18 - Nov' 20)
- Mock test papers

The scanner has been divided chapter wise to make it easier for you to follow. Do try to solve the questions before looking into the answers.


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Scanner – CA foundation The Companies Act, 2013

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When a company is registered, it is clothed with a legal personality. Explain.
(RTP May' 18)



When a company is registered, it is clothed with a legal personality. It comes to have almost the same rights and powers as a human being. Its existence is distinct and separate from that of its members. A company can own property, have bank account, raise loans, incur liabilities and enter into contracts.

- a. It is at law, a person different altogether from the subscribers to the memorandum of association. Its personality is distinct and separate from the personality of those who compose it.
- b. Even members can contract with company, acquire right against it or incur liability to it. For the debts of the company, only its creditors can sue it and not its members.

A company is capable of owning, enjoying and disposing of property in its own name. Although the capital and assets are contributed by the shareholders, the company becomes the owner of its capital and assets. The shareholders are not the private or joint owners of the company's property.



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' 18)**



One of the most distinguishing feature of a company is its being a separate entity from the shareholders and promoters who form it. This lends stability to the company form of business organization. In short, a company is brought into existence by a process of law and can be terminated or wound up or brought to an end only by a process of law. Its life is not impacted by the death, insolvency or retirement of any or all shareholder(s) or director(s). The provision for transferability or transmission of the shares helps to preserve the perpetual existence of a company by allowing the constitution and identity of shareholders to change.

In the above case the company had 5 members. All the members were going by car, met with an accident and all were dead. As the existence of the company is different from the existence of its members the company does not come to an end by the death of all its members. The company shall cease to exist only when it is wound up by a due process of law.

Therefore, even with the death of all members ABC (Pvt.) Ltd. does not cease to exist.



Examine the following whether they are correct or incorrect along with reasons:

- i. A company being an artificial person cannot own property and cannot sue or be sued.
- ii. A private limited company must have a minimum of two members, while a public limited company must have at least seven members. **(RTP May' 20)**



- i. The statement is incorrect: A company is an artificial person as it is created by a process other than natural birth. It is legal or judicial as it is created by law. It is a person since it is clothed with all the rights of an individual. Further, the company being a separate legal entity can own property, have banking account, raise loans, incur liabilities and enter into contracts. Even members can contract with company, acquire right against it or incur liability to it. It can sue and be sued in its own name. It can do everything which any natural person can do except be sent to jail, take an oath, marry or practice a learned profession. Hence, it is a legal person in its own sense.
- ii. The statement is correct: Section 3 of the Companies Act, 2013 deals with the basic requirement with respect to the constitution of the company. In the case of a public company, any 7 or more persons can form a company for any lawful purpose by subscribing their names to memorandum and complying with the requirements of this Act in respect of registration. In exactly the same way, 2 or more persons can form a private company.



Examine the following whether they are correct or incorrect along with reasons:

- a) A company being an artificial person cannot own property and cannot sue or be sued. **(RTP Nov' 18)**
- b) A private limited company must have a minimum of two members, while a public limited company must have at least seven members. **(RTP Nov' 18)/ (MT Oct' 18)**
- c) Affixing of Common seal on company's documents is compulsory. **(MT Oct' 18)**



A company being an artificial person cannot own property and cannot sue or be sued

The statement is Incorrect: A company is an artificial person as it is created by a process other than natural birth. It is legal or judicial as it is created by law. It is a person since it is clothed with all the rights of an individual.

Further, the company being a separate legal entity can own property, have banking account, raise loans, incur liabilities and enter into contracts. Even members can contract with company, acquire right against it or incur liability to it. It can sue and be sued in its own name. It can do everything which any natural person can do except be sent to jail, take an oath, marry or practice a learned profession. Hence, it is a legal person in its own sense.

A private limited company must have a minimum of two members, while a public limited company must have at least seven members.

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Affixing of Common seal on company's documents is compulsory.

The statement is incorrect: The common seal is a seal used by a corporation as the symbol of its incorporation. The Companies (Amendment) Act, 2015 has made the common seal optional by omitting the words “and a common seal” from Section 9 so as to provide an alternative mode of authorization for companies who opt not to have a common seal. This amendment provides that the documents which need to be authenticated by a common seal will be required to be so done, only if the company opts to have a common seal. In case a company does not have a common seal, the authorization shall be made by two directors or by a director and the Company Secretary, wherever the company has appointed a Company Secretary.



Naveen incorporated a “One Person Company” making his sister Navita as the nominee. Navita is leaving India permanently due to her marriage abroad. Due to this fact, she is withdrawing her consent of nomination in the said One Person Company. Taking into considerations the provisions of the Companies Act, 2013 answer the questions given below.

- i. If Navita is leaving India permanently, is it mandatory for her to withdraw her nomination in the said One Person Company?
- ii. If Navita maintained the status of Resident of India after her marriage, then can she continue her nomination in the said One Person Company? **(RTP May’ 20)**



As per Companies (Incorporation) Rules, 2014 only a

- Natural person
- Indian citizen and
- A resident of India

can be a member or a nominee of an OPC. The term resident of India mean a person who has stayed in India for a period of not less than 182 days in the immediately preceding financial year.

In the above case Naveen incorporated an OPC and nominated his sister Navita. Due to her marriage she had to leave India permanently. As the nominee must also be a resident of India she cannot continue to the nominee.

Thus

- i. It is mandatory for Navita to withdraw her nomination in the said OPC.
- ii. If she maintained her residential status she can continue to be the nominee of the OPC.



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' 19)/ (RTP May' 21)



As per Rule 3(7) of the Companies (Incorporation) Rules, 2014, an OPC cannot convert voluntarily into any kind of company unless two years have expired from the date of its incorporation, except threshold limit (paid up share capital) is increased beyond fifty lakh rupees or its average annual turnover during the relevant period exceeds two crore rupees. The term relevant period means a period of immediately preceding 3 consecutive financial years. In the instant case, Mr. Anil formed an OPC on 16th April, 2018 and its turnover for the financial year ended 31st March, 2019 was Rs. 2.25 Crores. Anil's friend Sunil wanted to invest and do decided to convert the OPC into a private company. As two years have not lapsed nor the company did not fail to fulfil the limits for capital and turnover the company cannot be converted.

Thus Mr. Anil cannot convert the OPC into a private limited company along with Sunil.



Explain the concept of "Dormant Company" as envisaged in the Companies Act, 2013. **(RTP May' 18)**



As per section 455 of the Companies Act, 2013 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 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 –

- a. payment of fees by a company to the Registrar;
- b. payments made by it to fulfil the requirements of this Act or any other law;
- c. allotment of shares to fulfil the requirements of this Act; and
- d. payments for maintenance of its office and records.



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. 20)**



The following are the significant points of a section 8 company:

- i. Formed for the promotion of commerce, art, science, religion, charity, protection of the environment, sports, etc.
- ii. Requirement of minimum share capital does not apply.
- iii. Uses its profits for the promotion of the objective for which formed.
- iv. Does not declare dividend to members.
- v. Operates under a special licence from the Central Government.
- vi. Need not use the word Ltd./ Pvt. Ltd. in its name and adopt a more suitable name such as club, chambers of commerce etc.
- vii. A partnership firm can be a member of Section 8 company.
- viii. Licence revoked if conditions contravened.
- ix. On revocation, the Central Government may direct it to – Converts its status and change its name – Wind – up – Amalgamate with another company having similar object.
- x. Can call its general meeting by giving a clear 14 days' notice instead of 21 days.
- xi. Requirement of minimum number of directors, independent directors etc. does not apply.
- xii. Need not constitute Nomination and Remuneration Committee and Shareholders Relationship Committee.



State whether a non-profit organization be registered as a company under the Companies Act, 2013? If so, what procedure does it have to adopt? **(RTP May' 18)/ (RTP May' 19)**



U/s 8 of the Companies Act, 2013 a non-profit organization may be registered as a company.

1. Such company is 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.
2. Such company shall apply to the Central Government who has the power to issue license for registering a section 8 company.
3. On such registration the company shall not use the word “ltd.” or “pvt. Ltd.” after its name.
4. The registrar shall on application register such person or association of persons as a company under this section.
5. On registration the company shall enjoy same privileges and obligations as of a limited company.



What do you mean by "Companies with charitable purpose" (section 8) under the Companies Act, 2013? Mention the conditions of the issue and revocation of the license of such company by the government. (Nov' 19)



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

- i. to promote the charitable objects of commerce, art, science, sports, education, research, social welfare, religion, charity, protection of environment etc.
- ii. 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.

1. Section 8 allows the Central Government to register such person or association of persons as a company.
2. On registration the company shall enjoy same privileges and obligations as of a limited company and need not use the word "Ltd. or Pvt. Ltd. after its name.
3. If the company contravenes any of the requirements or the conditions of this sections subject to which a license is issued or where the affairs of the company are conducted fraudulently, or violative of the objects of the company or prejudicial to public interest, the Central Government may by order revoke the license of the company.
4. On such revocation it shall convert into a private or a public company and inform the Registrar. The Registrar shall put 'Limited' or 'Private Limited' against the company's name in the register.
5. But before such revocation, the Central Government must give it a written notice of its intention to revoke the license and opportunity to be heard in the matter.



A company registered under section 8 of the Companies Act, 2013, earned huge profit during the financial year ended on 31st March, 2018 due to some favorable 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' 18/ MT Nov' 19)



U/s 8 of the Companies Act, 2013, a company may be registered as a non-profit organization. The objects of such company shall be:

- 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.

A company that is registered under section 8 of the Companies Act, 2013, is prohibited from the payment of any dividend to its members.

In the above case the company was registered under section 8. The company earned huge profits and some members wanted the company to distribute dividend. As per the object of section 8 such company is prohibited from declaring dividend.

Thus, the contention of members is incorrect.



Mike Limited company incorporated in India having Liaison office at Singapore. Explain in detail meaning of Foreign Company and analysis, 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' 21)**



As per 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 above case Mike Limited is a company incorporated in India, hence, it cannot be called as a foreign company. Even though, Liaison was officially established at Singapore, it would not be called as a foreign company as per the provisions of the Companies Act, 2013.

Thus Mike Ltd is not a foreign company.



Define OPC (One Person Company) and state the rules regarding its membership. Can it be converted into a non-profit company under Section 8 or a private company? (RTP Nov' 18)/ (May' 18)/ (MT Nov' 19)



Section 2(62) defines an OPC as a company which has only one person as a member.

Rules regarding its membership:

- i. Only one person as member.
- ii. 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.
- iii. 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.
- iv. Such other person may be given the right to withdraw his consent.
- v. 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.
- vi. Any such change in the name of the person shall not be deemed to be an alteration of the memorandum.
- vii. Only a natural person who is an Indian citizen and resident in India (person who has stayed in India for a period of not less than 182 days during the immediately preceding one calendar year)-
 - shall be eligible to incorporate a OPC;
 - shall be a nominee for the sole member of a OPC.
- viii. No person shall be eligible to incorporate more than one OPC or become nominee in more than one such company.
- ix. No minor shall become member or nominee of the OPC or can hold share with beneficial interest.

An OPC may be converted into a private or a public company after two years from the date of incorporation. However it can never convert into a section 8 company. If the paid up share capital of an OPC fifty lakh rupees or its average annual turnover during the relevant period exceeds two crore rupees such OPC must convert into a private or a public company.



Flora Fauna Limited was registered as a public company. There are 230 members in the company as noted below:

- a. Directors and their relatives 190
- b. Employees 15
- c. Ex-Employees (Shares were allotted when they were employees 10
- d. 5 couples holding shares jointly in the name of husband and wife (5×2) 10
- e. Others 5

The Board of Directors of the company propose to convert it into a private company. Also advise whether reduction in the number of members is necessary. (MT Mar' 19)/ (RTP May' 19)/ (MT May' 20)/ (Jan' 21)/ (MT)



According to section 2(68) of the Companies Act, 2013, "Private company" means a company having a minimum paid-up share capital as may be prescribed, and which by its articles, except in case of One Person Company, limits the number of its members to two hundred.

However, 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.

It is further provided that -

- A. persons who are in the employment of the company; and
- B. 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 members after the employment ceased

shall not be included in the number of members.

Further a public company may be converted into a private company if the number of members do not exceed 200 or is reduced to 200.

In the instant case, Flora Fauna Limited may be converted into a private company only if the total members of the company are limited to 200. The total number of members of the company is

i. Directors and their relatives	190
ii. 5 Couples	(5×1) 5
iii. Others	5
Total	200

Therefore, the company can convert into a private company without reducing the total number of members. there is no need for reduction in the number of members since existing number of members are 200 which does not exceed maximum limit of 200.



Alfa school started imparting education on 1st April, 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 clause due to which it was granted the status of a section 8 company under the Companies Act, 2013. Describe what powers can be exercised by the Central Government against the Alfa School, in such a case? (MT May' 20)/ (MT)



As per section 8 of the Companies Act, 2013, where a company incorporated not for profits breaches any of its objects the Central Government may revoke its license. On such a revocation:

- i. On revocation company must convert into a public or a private company. it shall inform the Registrar who shall put 'Limited' or 'Private Limited' against the company's name in the register.
- ii. The Central Government may, by order, if it is satisfied that it is essential in the public interest, direct that the company be wound up under this Act or amalgamated with another company registered under this section.
- iii. The Central Government is satisfied that it is essential in the public interest that the company registered under this section should be amalgamated with another company registered under this section and having similar objects, then,
- iv. However, no such order shall be made unless the company is given a reasonable opportunity of being heard.

In the above case Alfa School was a Section 8 company which had started violating the objects clause, hence in such a situation the Central Government may exercise any of the above powers.



SK Infrastructure Limited has a paid-up share capital divided into 6,00,000 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. **(Jan 21)/ (RTP May' 21)**



As per section 2(45) of the Companies Act, 2013, a Government Company means any company in which not less than 51% of the paid-up share capital is held by-

- i. The Central Government, or
- ii. any State Government or Governments, or
- iii. Partly by the Central Government and partly by one or more State Governments.

A company which is a subsidiary company of such a Government company is also a government company.

In the instant case, paid up share capital of SK Infrastructure Limited is 6,00,000 equity shares of 100 each. 200,000 equity shares are held by Central government and 1,20,000 equity shares are held by Government of Maharashtra. The holding of equity shares by both government is 3,20,000 which is more than 51% of total paid up equity shares.

Hence, SK Infrastructure Limited is a Government company.



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 stands 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' 20)/ (RTP May' 21)



As per 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. The term "significant influence" means control of at least 20% of total voting power or control of business decisions under an agreement.

In the given case, ABC Ltd. has allotted equity shares with voting rights to XYZ Limited of 15 crore, which is less than requisite control of 20% of total share capital (i.e. 100 crore) to have a significant influence of XYZ Ltd. Holding/allotment of non-convertible debentures has no relevance for ascertaining significant influence.

Thus ABC Ltd. and XYZ Ltd. are not associate companies as per the Companies Act, 2013 since the said requirement is not complied,



Popular Products Ltd. is a company incorporated in India, having a total Share Capital of 20 Crores. The Share capital comprises of 12 Lakh 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. (Nov' 19)



As per the provisions of section 2(46) a company is a holding company in relation to one or more means a company of which such companies are subsidiary companies.

As per section 2(87) a subsidiary company in relation to any other company means a company in which the holding company:

- i. Controls the composition of the Board of Directors
- ii. Exercises or controls more than one half of the total voting power either on 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.

In the present case, the total share capital of Popular Products Ltd. is 20 crores comprised of 12 Lakh equity shares and 8 Lakhs preference shares. Delight Products Ltd., Happy Products Ltd. and Cheerful Products Ltd together hold 8,50,000 shares (2,50,000+3,50,000+2,50,000) in Popular Products Ltd. Jovial Ltd. is the holding company of all above three companies. So, Jovial Ltd. along with its subsidiaries hold 8,50,000 shares in Popular Products Ltd. which amounts to less than one-half of its total share capital. Hence, Jovial Ltd. by virtue of share holding is not a holding company of Popular Products Ltd. Secondly, it is given that Jovial Ltd. controls the composition of directors of Popular Products Ltd.

Hence, Jovial Ltd. is a holding company of Popular Products Ltd. and not a subsidiary company.

(you can also make an assumption that all the shares held are equity)



The Articles of Association of XYZ Ltd. provides that Board of Directors has authority to issue bonds provided such issue is authorized by the shareholders by a necessary resolution in the general meeting of the company. The company was in dire need of funds and therefore, it issued the bonds to Mr. X without passing any such resolution in general meeting. Can Mr. X recover the money from the company? Decide referring the relevant provisions of the Companies Act, 2013. (RTP May' 18)



According to the Doctrine of Indoor Management, if an act is authorised by the articles or memorandum, an outsider is entitled to assume that all the detailed formalities for doing that act have been observed. In the case of the Royal British Bank V. Turquand the directors of R.B.B. Ltd. gave a bond to T. The articles empowered the directors to issue such bonds 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 bonds on the ground that he was entitled to assume that the resolution had been duly passed. This is the doctrine of indoor management, popularly known as Turquand Rule.

In the above case the articles of XYZ Ltd. states that the Board was authorized to issue bonds provided the company got the consent of the shareholders. The company was in need of funds and so without the consent of the shareholders issued bonds to X but without the consent of the shareholders. As it was the internal management X was under no obligation to check the internal management of the company

Thus Mr. X can recover the money from the company.



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’ 18)/ (MT Oct’ 18)/ (RTP May’ 20)**



The term ultra vires means “beyond the powers”. The rule of ultra vires is applicable to acts done in excess of the legal powers of the doers.

The fundamental rule of Company Law is 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. A company can be restrained from employing its fund for purposes other than those sanctioned by the memorandum. Likewise, it can be restrained from carrying on a trade different from the one it is authorised to carry on.

In the case of *Ashbury Railway Carriage and Iron Company V. Richie* the company was incorporated with the objects of:

- To make, sell or lend on hire railway carriages and wagons
- To carry on the work of mechanical engineers and general contractors.
- To purchase, lease, sell and work mines.
- To purchase and sell as merchants or agents, coal, timber, metals, etc.

The directors of the company contracted with Richie for financing the construction of railway line in Belgium. The company ratified the act of the directors by passing a special resolution. Later the company canceled the contract. Richie sued the company. The court held that the contract was void. The term general contractors was to be interpreted to mean work associated with mechanical engineers.

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. An act which is ultra vires the company being void, cannot be ratified by the shareholders of the company. Sometimes, act which is ultra vires can be regularised by ratifying it subsequently.



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 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. (MT Mar' 19)/ (Nov' 18)/ (MT)



The Doctrine of Indoor Management is the exception to the doctrine of constructive notice. The doctrine of constructive notice does not mean that outsiders are deemed to have notice of the internal affairs of the company. For instance, if an act is authorized by the articles or memorandum, an outsider is entitled to assume that all the detailed formalities for doing that act have been observed. They are entitled to assume that the acts of the directors or other officers of the company are validly performed, if they are within the scope of their apparent authority. So long as an act is valid under the articles, if done in a particular manner, an outsider dealing with the company is entitled to assume that it has been done in the manner required.

In the given question, Mr. X had to make the payment to the company. He made the payment to Mr. Z as Mr. Z informed him that the cashier and accountant were not present and he was in charge. Mr. Z also gave a receipt of the same to Mr. X. It will be rightful on part of Mr. X to assume that Mr. Z was also authorised to receive money on behalf of the company. Hence, Mr. X will be free from liability for payment of goods purchased from M/s ABC Limited, as he has paid amount due to an employee of the company.

Thus Mr. X has no liability to the company as the debt was already cleared.



F, 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 F as a pretended loan. This way, F 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 all the three companies may be disregarded. **(MT Mar' 19)/ (RTP Mar' 19)/ (MT)**

OR

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 bloc 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 all the three companies may be disregarded. **(MT Oct' 18)**



In the case of *Salomon V. Salomon & Co. Ltd.* the House of Lords laid down that a company is a person distinct and separate from its members, and therefore, has an independent separate legal existence from its members who have constituted the company. But under certain circumstances the separate entity of the company may be ignored by the courts. When that happens, the courts ignore the corporate entity of the company and look behind the corporate façade and hold the persons in control of the management of its affairs liable for the acts of the company. In the case of *Sir Dinshaw Maneckji Petit and Juggilal vs. Commissioner of Income Tax*, the court held that where a company is incorporated and formed by certain persons only for the purpose of evading taxes, the courts have discretion to disregard the corporate entity and tax the income in the hands of the appropriate assessee.

In the above case F had formed three companies purely and simply as a means of avoiding tax and the companies were nothing more than the façade of F himself. The whole idea was simply to split his income into three parts with a view to evade tax. No other business was done by the company but was created simply as a legal entity to ostensibly receive the dividend and interest and to hand them over to the assessee as pretended loans.

Thus the legal personality of the three private companies may be disregarded because the companies were formed only to avoid tax liability.



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' 18)



The term ultra vires means “beyond the powers”. The rule of ultra vires is applicable to acts done in excess of the legal powers of the doers. The fundamental rule of Company Law is 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. A company can be restrained from employing its fund for purposes other than those sanctioned by the memorandum. Likewise, it can be restrained from carrying on a trade different from the one it is authorised to carry on. In the case of *Ashbury Railway Carriage and Iron Company V. Richie* the court held that any contract which is ultra vires is void.

In the given case Ravi Private Limited borrowed 5 crore from Mudra Finance Ltd. This debt is ultra vires to the company, which signifies that Ravi Private Limited has borrowed the amount beyond the expressed limit prescribed in its memorandum. This act of the company can be said to be null and void. 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.

Therefore, the company Ravi Private Ltd. is liable to pay this debt amount upto the limit prescribed in the memorandum. So, Mudra Finance Ltd. can claim for the amount within the expressed limit prescribed in its memorandum.



State the limitations of the doctrine of indoor management under the Companies Act, 2013. (May' 18)



According to the Doctrine of Indoor Management, if an act is authorised by the articles or memorandum, an outsider is entitled to assume that all the detailed formalities for doing that act have been observed. Held in the case of Royal British Bank V. Turquand. However this rule is subject to certain limitation that is it is inapplicable in the following cases:

- i. **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.
- ii. **Suspicion of Irregularity:** The doctrine in no way, rewards those who behave negligently. Where the person dealing with the company is put upon an inquiry, for example, 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.
- iii. **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.



The persons (not being members) dealing with the company are always protected by the doctrine of indoor management. Explain. Also, explain when doctrine of Constructive Notice will apply. (MT May' 20)/ (Jan' 21)/ (MT)



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

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

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

The doctrine of indoor management is opposite to the doctrine of constructive notice.

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

Exceptions to Doctrine of Indoor Management (Applicability of doctrine of constructive notice) :

- i. **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.
- ii. **Suspicion of Irregularity:** The doctrine in no way, rewards those who behave negligently. Where the person dealing with the company is put upon an inquiry, for example, 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.
- iii. **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.



There are cases where company law disregards the principle of corporate personality or the principle that the company is a legal entity distinct from its shareholders or members. Elucidate. (Nov' 18)

OR

Some of the creditors of Pharmaceutical Appliances Ltd. have complained that the company was formed by the promoters only to defraud the creditors and circumvent the compliance of legal provisions of the Companies Act, 2013. In this context they seek your advice as to the meaning of corporate veil and when the promoters can be made personally liable for the debts of the company. (RTP Nov'



Corporate Veil refers to a legal concept whereby the company is identified separately from the members of the company. However, this veil can be lifted which 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 facade. Where the Courts ignore the company, and concern themselves directly with the members or managers, the corporate veil may be said to have been lifted. Only in appropriate circumstances, the Courts are willing to lift the corporate veil and that too, when questions of control are involved rather than merely a question of ownership.

Lifting of Corporate Veil

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 co-enemy or friend:** In the law relating to trading with the enemy where the test of control is adopted. The leading case in this point is **Daimler Co. Ltd. vs. Continental Tyre & Rubber Co.**, if the public interest is not likely to be in jeopardy, the Court may not be willing to crack the corporate shell. But it may rend the veil for ascertaining whether a company is an enemy company. It is true that, unlike a natural person, a company does not have mind or conscience; therefore, it cannot be a friend or foe.
2. **To protect revenue/tax:** In certain matters concerning the law of taxes, duties and stamps particularly where question of the controlling interest is in issue. Where corporate entity is used to **evade or circumvent tax**, the Court can disregard the corporate entity [**Juggilal vs. Commissioner of Income Tax**].

3. **To avoid a legal obligation:** Where it was found that 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 vs. The Associated Rubber Industries Ltd., Bhavnagar and another**).
4. **Company formed for fraud/improper conduct or to defeat law:** 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. vs. Horne**]



A, an assessee, had large income in the form of dividend and interest. In order to reduce his tax liability, he formed four private limited company and transferred his investments to them in exchange of their shares. The income earned by the companies was taken back by him as pretended loan. Can A be regarded as separate from the private limited company he formed? (Nov' 19)



The House of Lords in *Salomon Vs Salomon & Co. Ltd.* laid down that a company is a person distinct and separate from its members, and therefore, has an independent separate legal existence from its members who have constituted the company. However under certain circumstances the separate entity of the company may be ignored by the courts. In such a case the courts ignore the corporate entity of the company and look behind the corporate façade and hold the persons in control of the management of its affairs liable for the acts of the company. Where a company is incorporated and formed by certain persons only for the purpose of evading taxes, the courts have discretion to disregard the corporate entity and tax the income in the hands of the appropriate assessee. In *Dinshaw Maneckjee Petit* case it was held that the company was not a genuine company at all but merely the assessee himself disguised that the legal entity of a limited company. The assessee earned huge income by way of dividends and interest. So, he opened some companies and purchased their shares in exchange of his income by way of dividend and interest. This income was transferred back to assessee by way of loan. The court decided that the private companies were a sham and the corporate veil was lifted to decide the real owner of the income. In the instant case, the four private limited companies were formed by A, the assessee, purely and simply as a means of avoiding tax and the companies were nothing more than the façade of the assessee himself. Therefore, the whole idea of Mr. A was simply to split his income into four parts with a view to evade tax. No other business was done by the company. Hence, A cannot be regarded as separate from the private limited companies he formed.



The Object Clause of Memorandum of Association of ABC Pvt. Ltd. authorised 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 of trading. FSH Limited supplied fish to ABC Pvt. Ltd. worth Rs. 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. **(MT Aug' 18)**



The term ultra vires means “beyond the powers”. The rule of ultra vires is applicable to acts done in excess of the legal powers of the doers. The fundamental rule of Company Law is that the objects of a company as stated in its memorandum can be departed from only to the extent permitted by the Act. 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. this principle was laid down by the court in the case of Ashbury Railway Carriage and Iron Company V. Richie. The memorandum being a public document it is deemed that every person dealing with the company has knowledge about it.

In the above case the object clause of ABC Pvt. Ltd. authorized the company to carry on the business of trading in fruits and vegetables. The company decided to order fish for trading purpose. The members at the meeting negated the resolution on the grounds that it was ultra vires. The contract being ultra vires FSH Ltd. shall not have any remedies.

Therefore, the resolution passed by the Board of Director ABC Pvt. Limited for an ultra vires transaction is invalid. As a result of this, the transaction entered into the supply of fish with FSH Limited is void.



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? (MT Aug’ 18)



Under section 7(2) the Registrar shall on the basis of documents and information filed for the formation of a company, shall register all the documents and information and issue a certificate that the company is incorporated in the prescribed form to the effect that the proposed company is incorporated under this Act. The company becomes a legal entity from the date mentioned in the certificate of incorporation and continues to be so till it is wound up.

Effects of registration of a company

Section 9 of the Companies Act, 2013 provides that, from the date of incorporation mentioned in the certificate of incorporation, such of the subscribers to the Memorandum and all other persons, as may from time to time become members of the company, shall be a body corporate by the name contained in the memorandum, capable forthwith of exercising all the functions of an incorporated company under this Act and having perpetual succession with power to acquire, hold and dispose of property, both movable and immovable, tangible and intangible, to contract and to sue and be sued by the said name. Accordingly, when a company is registered and a certificate of incorporation is issued by the Registrar, three important consequences follow:

- a) the company becomes a distinct legal entity. Its life commences from the date mentioned in the certificate of incorporation capable of entering into contracts in its own name, acquiring, holding and disposing of property of any nature whatsoever and capable of suing and being sued in its own name.
- b) it acquires a life of perpetual existence by the doctrine of succession. The members may come and go, but it goes on forever, unless it is wound up.
- c) Its property is not the property of the shareholders. The shareholders have a right to share in the profits of the company as and when declared either as dividend or as bonus shares.

Likewise any liability of the company is not the liability of the individual shareholders.



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. **(MT Aug' 18)**



As per section 7(7) of the Companies Act, 2013, where a company has been 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, direct that liability of the members shall be unlimited.

Before making any order,—

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

In the above case **FAREB Ltd.** was incorporated by the acquisition of **FAREB & Co.** a partnership firm which was engaged in illegal activities. The promoters furnished wrong incorporation and suppressed material facts at the time of incorporation. Some members from the public approached the NCLT against the company and the NCLT is about to pass orders to make the liability unlimited.

Hence, the order of NCLT will be legal.



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 25,00,000 in name of the company.

The Lender agreed and provided the above 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 providing such loan hence company 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? (Nov' 19)



According to the doctrine of indoor management, as laid down in the case of Royal British Bank V. Turquand persons dealing with the company need not inquire whether internal proceedings relating to the contract are followed correctly, once they are satisfied that the transaction is in accordance with the memorandum and articles of association. Outsiders are not required to enquire about the internal management. They are entitled to take it for granted that the company had gone through all these proceedings in a regular manner. The doctrine protects the outsiders from the company and states that the people are entitled to presume that internal proceedings are as per documents submitted with the Registrar of Companies. If not for the doctrine, the company could escape creditors by denying the authority of officials to act on its behalf.

In the above case Sound Syndicate Ltd. is authorized by its articles to borrow loan through the managing agents. Mr. Liddle the director of the company took a loan in the name of the company. later the company refused to repay the money on the grounds that no resolution to authorise such payment was passed. As it is not the duty of the outsider to check whether the company has passed the resolution or not he is not liable for the company's negligence.

Thus, the contention of the company is not correct and they are liable to repay the money back.



The Memorandum of Association is a charter of a company". Discuss. Also explain in brief the contents of Memorandum of Association. (Nov' 19)



The Memorandum of Association of company is in fact its charter; it defines its constitution and the scope of the powers of the company with which it has been established under the Act. It is the very foundation on which the whole edifice of the company is built.

Object of registering a memorandum of association:

- It contains the object for which the company is formed and therefore identifies the possible scope of its operations beyond which its actions cannot go.
- It enables shareholders, creditors and all those who deal with company to know what its powers are and what activities it can engage in.

A memorandum is a public document under Section 399 of the Companies Act, 2013. Consequently, every person entering into a contract with the company is presumed to have the knowledge of the conditions contained therein.

The shareholders must know the purposes for which his money can be used by the company and what risks he is taking in making the investment.

A company cannot depart from the provisions contained in the memorandum however imperative may be the necessity for the departure. It cannot enter into a contract or engage in any trade or business, which is beyond the power conferred on it by the memorandum. If it does so, it would be ultra vires the company and void.

The memorandum of a company shall state—

- i. the name of the company (Name Clause) with the last word "Limited" in the case of a public limited company, or the last words "Private Limited" in the case of a private limited company. This clause is not applicable on the companies formed under section 8 of the Act.
- ii. the State in which the registered office of the company (Registered Office clause) is to be situated;
- iii. the objects for which the company is proposed to be incorporated and any matter considered necessary in furtherance thereof (Object clause);
- iv. the liability of members of the company (Liability clause), whether limited or unlimited
- v. the amount of authorized capital (Capital Clause) divided into share of fixed amounts and the number of shares with the subscribers to the memorandum have agreed to take, indicated opposite their names, which shall not be less than one share. A company not having share capital need not have this clause.
- vi. the desire of the subscribers to be formed into a company. The Memorandum shall conclude with the association clause. Every subscriber to the Memorandum shall take at least one share, and shall write against his name, the number of shares taken by him.