

TopYug Educations**CA FOUNDATION – BUSINESS LAWS****SUGGESTED ANSWERS for TEST 7 – THE COMPANIES ACT, 2013****Answer any 5 questions. Each question carries 4 marks each. Duration – 50 Mins**

1. 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 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.

Answer:

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.

As per the case of *the Royal British Bank vs. 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.

Since, the given question is based on the above facts, accordingly here in this case Mr.X can recover the money from the company considering that all required formalities for the passing of the resolution have been duly complied.

2. 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?

Answer:

The most distinguishing feature of a company is its being a separate entity from the shareholders and promoters who form it. This lends stability and perpetuity 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 present case, ABC Pvt. Ltd. does not cease to exist even by the death of all its shareholders. The legal process will be for the successors of the deceased shareholders to get the shares registered in their names by way of the process which is called "transmission of shares". The company will cease to exist only when it is wound up by a due process of law.

Therefore, even with the death of all members (i.e. 5), ABC (Pvt.) Ltd. does not cease to exist.

3. 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?

Answer:

As per Section 2(62) of the Companies Act, 2013, one person company (OPC) is a company which has only one person as a member.

Rules regarding its membership:

- Only one person as member.
- 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 and resident in India (person who has stayed in India for a period of not less than 182 days during the immediately preceding one financial year)-
 - shall be eligible to incorporate a OPC;
 - shall be a nominee for the 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.

OPC cannot be incorporated or converted into a company under section 8 of the Act. Though it may be converted to private or public companies in certain cases. OPC cannot convert voluntarily into any kind of company unless two years have expired from the date of incorporation, except where the paid up share capital is increased beyond fifty lakh rupees or its average annual turnover during the relevant period exceeds two crore rupees.

4. 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.

Answer:

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.

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. 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.

The problem asked in the question is based upon the aforesaid facts. The three companies were formed by 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. F was simply to split his income into three parts with a view to evade tax. No other business was done by the company.

The legal personality of the three private companies may be disregarded because the companies were formed only to avoid tax liability. It carried on no other business, 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. The same was upheld in *Re Sir Dinshaw Maneckji Petit case as well*.

5. 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. Advise whether reduction in the number of members is necessary.

Answer:

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.

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.

Total Number of members

(i)	Directors and their relatives	190
(ii)	5 Couples (5*1)	5

(iii)	Others	5
	Total	200

Therefore, 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.

6. Examine the following whether they are correct or incorrect along with reasons:
- A company being an artificial person cannot own property and cannot sue or be sued.
 - A private limited company must have a minimum of two members, while a public limited company must have at least seven members.

Answer:

(a) Incorrect

A company is an artificial person as it is created by a process of law other than natural birth. It is legal or judicial person 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 bank 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.

(b) 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.

GOOD LUCK !