

## EXECUTIVE PROGRAMME EXAMINATION

JUNE 2009

### GENERAL AND COMMERCIAL LAWS

*Time allowed : 3 hours*

*Maximum marks : 100*

**NOTE :** Answer SIX questions including Question No. 1 which is **COMPULSORY**.

#### **Question 1**

- (a) "A declaration of fundamental rights is meaningless unless there is an effective judicial remedy for their enforcement." Comment on this statement explaining the judicial remedies which the Constitution of India provides. (8 marks)
- (b) When and under what circumstances can the Parliament legislate on matters enumerated in the State List ? Discuss. (6 marks)
- (c) Briefly mention internal and external aids to interpretation of statute. (6 marks)

#### **Answer 1(a)**

It is true that a declaration of fundamental rights is meaningless unless there is an effective machinery for the enforcement of rights. It is a well known rule of law that where there is a right there shall be remedy (*ubi jus ibi remedium*) and if rights are given without there being a remedy for their enforcement, they are of no use. While remedies are available in the Constitution and under the ordinary laws, Article 32 makes it a fundamental right that a person whose fundamental right is violated has the right to move the Supreme Court by appropriate proceedings for the enforcement of this fundamental right. Our constitution makers having incorporated a long list of fundamental rights have also provided for an effective remedy for the enforcement of these rights under Article 32 of the Constitution. Article 32 is itself a fundamental right. It is remedial and not substantive in nature. This Article has been called as the heart and soul of the Constitution.

Article 32(1) of the Constitution of India guarantees the right to move the Supreme Court by "appropriate proceedings" for the enforcement of fundamental rights conferred by Part III of the Constitution.

The right conferred under Article 32 being a fundamental right cannot be abrogated, abridged or taken away by the Act of the legislature.

It is really a far reaching provision in the sense that a person need not first exhaust the other remedies and then move the Supreme Court. On the other hand, he can directly raise the matter before highest Court of the land under Article 32(2) which empowers the Supreme Court to issue directions or orders or following writs. :

- (i) Habeas Corpus;
- (ii) Mandamus
- (iii) Quo-Warranto
- (iv) Prohibition and
- (v) Certiorari

whichever may be appropriate for the enforcement of the fundamental right the violation of which is alleged. This power of the Supreme Court to issue directions, etc., may also be assigned to other Courts by Parliament without affecting the powers of the Supreme Court.

The right to move the Supreme Court is itself a guarantee right and the significance of this has been assessed by Gajendragadkar, J. in the following words:

“The fundamental right to move this Court can therefore be appropriately described as the cornerstone of the democratic edifice raised by the Constitution. That is why it is natural that this Court should, in the words of Patanjali Sastri, J., regard itself ‘as the protector and guarantor of fundamental rights’, and should declare that “it cannot, consistently with the responsibility laid upon it, refuse to entertain applications seeking protection against infringements of such rights. In discharging the duties assigned to it, this Court has to play the role of ‘sentinel on the qui vive’ (*State of Madras v. V.G. Row*, AIR 1952 SC 196) and it must always regard it as its solemn duty to protect the said fundamental rights ‘zealously and vigilantly’ (*Daryao v. State of U.P.*, AIR 1961 SC 1457).

The right guaranteed by Article 32 shall not be suspended except as provided in the Constitution. Constitution does not contemplate such suspension except by way of President’s order under Article 359 when a proclamation of Emergency is in force.

### **Answer 1(b)**

Although the State Legislatures have the exclusive powers to make laws with respect to the subjects included in State list and the Parliament has no power to encroach upon them, Our constitution makes a few exceptions to this general rule by authorizing Parliament to make laws even on the subjects enumerated in State list. These exceptions are as follows:

- (i) *In the National Interest (Article 249)* : Parliament can make a law with respect to a matter enumerated in the State list if the Council of the States declares by a resolution supported by 2/3rds of its members present and voting that it is necessary or expedient in the national interest that Parliament should make a law on that matter. By such declaration, the Parliament gets the authority to legislate on that matter for the whole or part of the country so long as the resolution of Council of State remains in force. Such a resolution normally lasts for a year. However it may be renewed as many times as may be necessary but not exceeding one year at a time.
- (ii) *During a proclamation of Emergency (Article 250)* : According to Article 250 while the proclamation of emergency is in operation, the Parliament shall have the power to make laws for the whole or any part of the territory of India with respect to all matters in the State list. Such a law, however, shall cease to have effect on the expiration of six months after the proclamation of emergency ceases to operate.
- (iii) *On the request of two or more States (Article 252)* : According to Article 252, if the legislature of two or more states pass a resolution to the effect that it is desirable to have a law passed by Parliament on any matters in the State List so that there should be a common legislation applicable to all such States, it

shall be lawful for Parliament to make law regulating that matter. Any other state may adopt such a law by passing a resolution to that effect. Such law can be amended or repealed by the Act of Parliament.

- (iv) *For enforcing treaties and international agreements (Article 253)* : Article 253 confers on union Parliament exclusive power to make laws in any list with respect to foreign affairs and entering into treaties and agreements with foreign countries and implementing of the treaties, agreements and conventions with foreign countries. But laws enacted for the enforcement of treaties cannot infringe fundamental rights.
- (v) *Failure of Constitutional Machinery in state [Article 356, 357]*: Whenever Governor of a State reports to the President that there is a breakdown of constitutional machinery in that State and functions cannot be carried out as per constitution in that State, the powers of the State Legislature are to be exercised by Parliament. President can confer on the Parliament the power to make laws for the States. Parliament may also authorize the President to delegate such power to any other authority as may be specified by him [Article 357(1(a))].

#### **Answer 1(c)**

For interpreting any provisions of any statute, it is permissible to consider internal and external evidence of such statute. They are stated in brief as follows:

- A. Internal Aids** : The following may be taken into consideration for interpretation of any statute as internal aids.
- (i) *Title of the Act* : It is a part of the statute and may be helpful to interpret the provisions of such statute. The long title sets out in general terms, the purpose of Act and it precedes the preamble
  - (ii) *Preamble*: The preamble of a statute is not part thereof but contains generally the motive or inducement thereof. Preamble is to be considered, for it is the key to open the meaning of the makers of the Act and the mischief it was intended to remedy.
  - (iii) *Heading and Title of a Chapter* : In *Frick India Ltd. v. Union of India* (AIR 1990 SC 689), the Supreme Court held that the heading prefixed to Section or entries cannot control the plain words of the provision, they cannot also be referred to for the purpose of construing the provision when words used are clear. Only in the case of ambiguity or doubt the heading or sub-heading may be referred to as an aid for construing the provisions but even in such case aid could not be used for cutting down the wide application of clear words used in the provision.
  - (iv) *Marginal Notes* : The marginal notes cannot be invoked for interpretation where meaning is clear. But in the case of ambiguity, it is helpful for the interpretation of the provisions.
  - (v) *Interpretation Clauses* : It is common to find in statutes “definitions” of certain words and expressions used elsewhere in the body of the statute. The object of such a definition is to avoid the necessity of frequent repetitions in describing all the subject-matter to which the word or expression so defined is intended to apply.

- (vi) *Proviso* : The proper function of proviso is to provide exception of the general rule given in the Section.
- (vii) *Illustrations & Explanations* : Illustrations are part of the statute and useful to indicate the intention of the legislature regarding the Section or provision. An explanation explains the meaning of words contained in the Section.
- (viii) *Schedules* forms part of the statute and must be read together with it for all purposes of construction.

**B. External Aids** : In the case of ambiguity, for the sake of interpretation of the provisions of the statute, the external aids may be considered like parliamentary history of the statute, reference to report of committee which was constituted to enact the statute, etc. It is well accepted legislative practice to incorporate by reference, if the legislature so chooses, the provisions of some other Acts in so far as they are relevant for the purposes of and in furtherance of the scheme of subjects of the Act. In the case of the ambiguity of the words dictionaries may be useful. Foreign judicial decisions may be useful in peculiar situations.

### Question 2

*Write short notes on any four of the following :*

- (i) *Expert opinion*
- (ii) *Doctrine of feeding the grant by estoppel*
- (iii) *Doctrine of lis pendens*
- (iv) *E-governance*
- (v) *Adjudicating officer.* (4 marks each)

### Answer 2(i)

#### Expert Opinion

According to Section 45 of the Indian Evidence Act, 1872, opinions of the persons who are experts or have special knowledge or skill in any particular field are called expert opinion. Opinions of the experts are admissible when the question in issue is such which can be determined only by special training or experience.

*Who is an expert* : As per Section 45, a person who is specially skilled is an expert for the purpose of this section. The opinions of experts are relevant upon a point of:

- (i) Foreign law
- (ii) Science
- (iii) Art
- (iv) Identity of handwriting
- (v) Identity of finger impressions.

### Answer 2(ii)

#### Doctrine of feeding the grant by estoppel

This means that if a man who has no title to a property grants it by conveyance

which would carry the legal estate and if he subsequently acquires an interest sufficient to satisfy the grant, the estate instantly passes. An estoppel arises against him by reasons of his conduct and the law obliges him to feed that estoppel by reason of his subsequent acquisition. Section 43 of the Transfer of Property Act, 1882 provides that where a person fraudulently or erroneously represents that he is authorized to transfer certain immovable property and professes to transfer such property for consideration, such transfer shall at the option of the transferee, operate on any interest which the transferor may acquire in such property at any time during which the contract of transfer subsists.

Nothing in this section shall impair the rights of a transferee in good faith for consideration, without notice of the existence of the said option.

### **Essentials**

- (i) There was a representation, fraudulent or erroneous;
- (ii) It was to the effect that the transferor is entitled to transfer the immovable property;
- (iii) The transferor is found to have subsequently acquired the interest which he professed to transfer;
- (iv) The transfer of property was for consideration;
- (v) The transferee has not rescinded the contract; and
- (vi) The transferee acted in good faith for consideration and without notice of the rights under the prior transfer.

### **Answer 2(iii)**

#### ***Doctrine of Lis pendens***

Section 52 of the Transfer of Property Act, 1882 embodies the doctrine of *lis pendens*, as expressed in the maxim "*ut lite pendente nihil innovetur*" which means that nothing new should be introduced in a pending litigation. Section 52 states that during the pendency of a suit in a court of law, property which is subject to litigation cannot be transferred. It actually means that the property may be transferred but this transfer is subject to the rights that are created by a Court's decree.

### **Essentials**

- (i) There must be a suit or proceeding in a court of competent jurisdiction;
- (ii) The suit or proceeding must be one in which right to immovable property is directly and specifically in question.
- (iii) The suit or proceeding must not be collusive.
- (iv) There must be transfer of or otherwise dealing with the property in dispute by any party to the litigation.
- (v) Such transfer must affect the rights of the other party that may ultimately accrue under the terms of the decree or order.

A suit in foreign Court cannot operate as *lis pendens*. The doctrine of *lis pendens* does not apply to movables.

**Answer 2(iv)****E-governance**

Section 4 of the Information Technology Act, 2000 grants legal recognition to electronic records by laying down that where (by any law) “information” or any other matter is to be in:

- (a) writing or
- (b) typewritten form or
- (c) printed form,

then, such requirement is satisfied, if such information or matter is:

- (i) rendered or made available in an electronic form; and
- (ii) accessible, so as to be usable for a subsequent reference.

*Private transactions*

Section 4 of the said Act practically equates electronic record with a manual or typed or printed record. Section 5 of the said Act proceeds to achieve the same object in regard to signature by laying down that where any law provides that information or any other matter shall be “signed”, such requirement is satisfied by authentication through digital signature in the prescribed manner.

*Public records*

Section 6 of the said Act proceeds to bring in the regime of electronic records and digital signature in public records, by making an analogous provision which grants recognition to electronic records and digital signatures, in cases where any law provides for

- (a) the filing of any form, application or any other document with a Governmental office or agency or
- (b) the grant of any licence, permit etc. or
- (c) the receipt or payment of money in a particular manner.

**Answer 2(v)****Adjudicating officer**

According to Section 46 of the Information Technology Act, 2000 an adjudication officer is to be appointed by the Central Government for adjudging whether any person has committed a contravention of the Act or of any rule, regulation, direction or order issued under the Act. He may impose penalty or award compensation in accordance with the provisions of the relevant section.

In adjudging the quantum of compensation the following factors are to be taken into account by the adjudication officer:

- (a) the amount of gain or unfair advantage (wherever quantifiable), made as a result of the default;

- (b) the amount of loss caused to any person as a result of the default; and
- (c) the repetitive nature of the default

### Question 3

Distinguish between **any four** of the following :

- (i) 'Public key' and 'private key'.
- (ii) 'Vested interest' and 'contingent interest'.
- (iii) 'Complaint' and 'FIR'.
- (iv) 'Res judicata' and 'stay of suits'.
- (v) 'Computer' and 'computer network'. (4 marks each)

#### Answer 3(i)

##### 'Public Key' and 'Private Key'

According to Section 2(1) (zd) of the Information Technology Act, 2000, the term 'public key' means "the key of a key pair, used to verify a digital signature and listed in the Digital Signature Certificate." On the other hand the term 'private key' as defined under Section 2(1) (zc) of the Information Technology Act, 2000, means "the key of a key pair, used to create a digital signature."

#### Answer 3(ii)

##### 'Vested Interest' and 'Contingent Interest'

1. When an interest is vested the transfer is complete whereas the contingent interest is dependant upon the fulfilment of some conditions which may or may not happen.
2. A vested interest takes effect from the date of transfer. A contingent interest in order to become vested is conditioned by a contingency which may not occur.
3. A vested interest cannot be defeated by the death of the transferee before he obtains possession. A contingent interest may fail in case of the death of transferee before the fulfilment of condition.
4. Since vested interest is not circumscribed by any limitation which derogates from the completeness of the grant, it logically follows that a vested interest is transferable as well as heritable. If, therefore, a transferee of the vested interest dies before actual enjoyment, it will devolve on his legal heirs. A contingent interest, on the other hand, cannot be inherited though it may be transferred coupled with limitation regarding fulfilment of a condition.

#### Answer 3(iii)

##### 'Complaint' and 'FIR'

- (a) In complaint the allegation is made orally or in writing to a Magistrate, but the report of cognizable offence is given to an officer in charge of a Police Station, which is called FIR.

- (b) A complaint may relate to non-cognizable offence, whereas FIR must relate to a cognizable offence on the face of it.
- (c) A magistrate takes cognizance of an offence on a complaint made to him but he cannot do so on a FIR.
- (d) A complaint does not include the report of the police officer; FIR may be lodged by any body including a police officer with respect to cognizable offence.

**Answer 3(iv)****'Res judicata' and 'stay of suits'**

- (i) *res judicata* applies to a matter adjudicated upon ( *res judicatum*), but stay of suits applies to a matter pending trial (*sub judice*) and
- (ii) *res judicata* bars the trial of a suit or an issue which has been decided in a former suit, stay of suits bars the trial of a suit which is pending decision in a previously instituted suit.

**Answer 3(v)****'Computer' and 'Computer network'**

As per Section 2(1) (i) of the Information Technology Act, 2000 "computer" means any electronic, magnetic, optical or other high-speed data processing device or system which performs logical, arithmetic, and memory functions, by manipulations of electronic, magnetic or optical impulses, and includes all input, output, processing, storage, computer software, or communication facilities which are connected or related to the computer in a computer system or computer network

As per Section 2(1) (j) of the said Act, "computer network" means the interconnection of one or more computers through -

- (i) the use of satellite, microwave, terrestrial line or other communication media; and
- (ii) terminals or a complex consisting of two or more interconnected computers, whether or not the interconnection is continuously maintained.

**Question 4**

Attempt **any four** of the following :

- (i) State the modes of cancellation of adhesive stamps.
- (ii) State the documents of which registration is optional.
- (iii) Specify the categories of information that have been exempted from disclosure under the Right to Information Act, 2005.
- (iv) What are the cyber offences under the Information Technology Act, 2000 ?
- (v) "Where once time has begun to run, no subsequent disability or inability to institute a suit or make an application can stop it." Discuss.
- (vi) Explain the maxim *damnum sine injuria* under the law of torts.

(4 marks each)



**Answer 4(i)**

Section 12(3) of the Indian Stamp Act, 1899 provides that the cancellation of an adhesive stamp may be done by the person concerned by writing on or across the stamp his name or initials or the name or initials of his firm with the true date of his so writing, or in any other effectual manner.

In *Mahadeo Koeri v. Sheoraj Ram Teli* AIR 1919 All 196, it was held that a stamp may be treated as having been effectively cancelled by merely drawing a line across it.

**Answer 4(ii)**

Section 18 of the Registration Act, 1908 specifies documents, registration of which is optional. It provides that any of the following documents may be registered under this Act, namely:

- (a) instruments (other than instruments of gift and wills) which purport or operate to create, declare, assign, limit or extinguish, whether in present or in future, any right, title or interest whether vested or contingent, of value less than one hundred rupees, to or in immovable property;
- (b) instruments acknowledging the receipt or payment of any consideration on account of the creation, declaration, assignment; limitation or extinction of any such right, title or interest;
- (c) leases of immovable property for any term not exceeding one year and leases exempted under Section 17;
- (d) instruments transferring or assigning any decree or order of a court or any award when such decree or order or award purports or operates to create, declare, assign, limit or extinguish, whether in present or in future, any right, title or interest, whether vested or contingent of a value less than one hundred rupees, to or in immovable property;
- (e) instruments (other than wills) which purport or operate to create declare, assign, limit or extinguish any right, title or interest to or in movable property;
- (f) wills; and
- (g) other documents not required by Section 17 to be registered.

**Answer 4(iii)**

Following categories of information have been exempted from disclosure under Section 8 of the Right to Information Act, 2005:

- Where disclosure prejudicially affects the sovereignty and integrity of India, the security, strategic, scientific or economic interests of the State, relation with foreign State or lead to incitement of an offence;
- Information which has been expressly forbidden by any court or tribunal or the disclosure of which may constitute contempt of court;
- Where disclosure would cause a breach of privilege of Parliament or the State Legislature;

- Information including commercial confidence, trade secrets or intellectual property, where disclosure would harm competitive position of a third party, or available to a person in his fiduciary relationship, unless larger public interest so warrants;
- Information received in confidence from a foreign government;
- Information the disclosure of which endangers life or physical safety of any person or identifies confidential source of information or assistance;
- Information that would impede the process of investigation or apprehension or prosecution of offenders;
- Cabinet papers including records of deliberations of the Council of Ministers, Secretaries and other officers:

Provided that the decisions of Council of Ministers, the reasons thereof, and the material on the basis of which the decisions were taken shall be made public after the decision has been taken, and the matter is complete, or over:

Provided further that those matters which come under the exemptions specified in this section shall not be disclosed;

Personal information which would cause invasion of the privacy unless larger public interest justifies it.

#### **Answer 4(iv)**

According to the Information Technology Act, 2000, cyber offences are classified as follows:

- (i) Tampering with computer source documents (Section 65)
- (ii) Hacking with computer system (Section 66);
- (iii) Publishing of obscene information (Section 67);
- (iv) Failure to comply with controller's Directions (Section 68);
- (v) Failure to decrypt information (Section 69);
- (vi) Breaking into protection system (Section 70);
- (vii) Misrepresentation before Controller or Certifying authority (Section 71);
- (viii) Breach of confidentiality or privacy (Section 72);
- (ix) Publishing erroneous digital signature certificate (Section 73);
- (x) When a person knowingly creates, publishes or otherwise makes available a digital signature certificate for any fraudulent or unlawful purpose (Section 74).

#### **Answer 4(v)**

According to Section 9 of the Limitation Act, 1963, where once time has begun to run, no subsequent disability or inability to institute a suit or make an application can stop it provided that where letters of administration to the estate of a creditor have been granted to his debtor, the running of the period of limitation for a suit to recover debt shall be suspended while the administration continues.

The rule of this Section is based on the English dictum. "Time when once it has commenced to run in any case will not cease to be so by reason of any subsequent event". Thus, when any of the statutes of limitation has begun to run, no subsequent disability or inability will stop its running.

The applicability of this Section is limited to suits and applications only and does not apply to appeals unless the case fell within any of the exceptions provided in the Act itself.

For the applicability of Section 9 it is essential that the cause of action or the right to move the application must continue to exist and subsisting on the date on which a particular application is made. If a right itself had been taken away by some subsequent event, no question of bar of limitation will arise as the starting point of limitation for that particular application will be deemed not to have been commenced.

#### **Answer 4(vi)**

***Damnum sine injuria*** : The maxim means that in a given case, a man may have suffered damage and yet have no action in tort, because the damage is not to an interest protected by the law of torts. Therefore causing damage, however, substantial to another person is not actionable in law unless there is also a violation of legal right of the plaintiff. Common examples are where the damage results from an act done in the exercise of legal rights.

In Gloucester Grammar School Case (1410) Y. B.Hill.11 Hen, 4 of 47, pp. 21, 36, A owned a School and at A's Neighborhood 'B' opened another school in which B reduced the fees of the students. All the students of A's school joined B's school; hence A was in the economic loss. But it was not actionable because there was no violation of legal rights of A.

#### **Question 5**

*State, with reasons in brief, whether the following statements are correct or incorrect:*

- (i) *In computing the period of limitation for an application to set aside an award, the time required for obtaining a copy of the award shall not be excluded.*
- (ii) *A document executed by several persons at different times may be presented for registration and re-registration within six months from the date of each execution.*
- (iii) *Anubhav sells a property to Balwant for Rs.5 lakh which is subject to a mortgage to Charu for Rs. 10 lakh and unpaid interest of Rs.2 lakh. Stamp duty is payable on Rs.17 lakh.*
- (iv) *Suits for compensation for false imprisonment can be filed within two years from the date when the imprisonment ends.*
- (v) *Article 53 of the Constitution of India lays down that the executive powers of the Union shall be vested in the President of India.*
- (vi) *The rule of 'harmonious construction' is the best rule of interpretation of any provision of any statute.*
- (vii) *Under certain circumstances, the court may award damages in addition to specific enforcement of the contract.*

(viii) *Generally orders passed by the court under the Code of Civil Procedure, 1908 are not appealable but there are certain exceptions to it. (2 marks each)*

**Answer 5(i)**

**Incorrect**

Section 12(4) of Limitation Act, 1963 provides that in computing the period of limitation for an application to set aside an award, the time requisite for obtaining a copy of the award shall be excluded.

**Answer 5(ii)**

**Incorrect**

Section 24 of the Registration Act, 1908, a document executed by several persons at different times may be presented for registration and re-registration within four months from the date of each execution.

**Answer 5(iii)**

**Correct**

The explanation appended to Section 24 of the Indian Stamp Act, 1899 inter alia provides that in the case of sale of property subject to mortgage or other encumbrances, any unpaid mortgage money or money charged together with the interest, if any, due on the same shall be deemed to be part of the consideration for the sale.

**Answer 5(iv)**

**Incorrect**

Under the Limitation Act, 1963, suits for compensation for false imprisonment can be filed within one year from the date when the imprisonment ends.

**Answer 5(v)**

**Correct**

The President of India shall be the head of the 'executive power' of the Union.

**Answer 5(vi)**

**Correct**

It provides that a statute must be read as a whole and one provision of the Act should be construed with reference to other provisions in the same Act so as to make consistent enactment of the whole statute.

**Answer 5(vii)**

**Correct**

Section 21 of the Specific Relief Act, 1963 provides that in a suit of specific performance of contract, the plaintiff may also claim compensation for its breach either in addition or in substitution of such performance.

**Answer 5(viii)****Correct**

The exceptions are provided under Section 104 and Order 43 Rule 1 of the Civil Procedure Code, 1908 specifying the categories of orders which are appealable.

**Question 6**

- (a) Choose the most appropriate answer from the given options in respect of the following :
- (i) The Constitution of India came into force on —
    - (a) 26th November, 1949
    - (b) 15th August, 1947
    - (c) 26th January, 1947
    - (d) 26th January, 1950.
  - (ii) The right to alienate the mortgaged property without intervention of the court is available to the mortgagee in the case —
    - (a) Where the mortgagee is government
    - (b) Where there is English mortgage
    - (c) Where there is mortgage by conditional sale
    - (d) Under both (a) and (b).
  - (iii) The relief regarding recovery of possession of immovable property is available under —
    - (a) Provisions of the Code of Civil Procedure, 1908
    - (b) Provisions of the Specific Relief Act, 1963
    - (c) Provisions of the Code of Criminal Procedure, 1973
    - (d) Both (a) and (b).
  - (iv) In the transfer of property with condition, the condition is void and transfer is valid —
    - (a) Where transfer is made with void condition
    - (b) Where transfer is made with the condition restraining absolutely future transfer of such property
    - (c) Where transfer is made absolutely with the condition restraining enjoyment of such property
    - (d) Both (b) and (c).
  - (v) Section 20 of the Right to Information Act, 2005 imposes penalty on a public information officer for failing to provide information —
    - (a) Rs. 250 per day
    - (b) Rs.250 per day to the extent of maximum Rs. 50,000
    - (c) Rs.300 per day to the extent of maximum Rs. 25,000
    - (d) Rs.250 per day to the extent of maximum Rs. 25,000.

- (vi) *The Chief Judicial Magistrate is empowered to pass —*
- (a) *Any sentence authorised by law*
  - (b) *Any sentence except a sentence of death*
  - (c) *Any sentence except a sentence of death, life imprisonment or imprisonment for a term exceeding seven years*
  - (d) *Any sentence except a sentence of death and life imprisonment.*
- (vii) *The definition of ‘decree’ as given under section 2 of the Code of Civil Procedure, 1908 includes —*
- (a) *An ‘award’ passed by the arbitral tribunal under the Arbitration and Conciliation Act, 1996*
  - (b) *Rejection of plaint under Order 7, Rule 11 of the Code of Civil Procedure, 1908*
  - (c) *Adjudication of any question raised by any party to the decree during execution proceedings under section 47 of the Code of Civil Procedure, 1908*
  - (d) *An order of which appeal lies like an order.*
- (viii) *A magistrate may take cognizance of any offence upon —*
- (a) *His own knowledge*
  - (b) *The information of police officer*
  - (c) *The information of any person other than police officer*
  - (d) *His own knowledge, police report and complaint or information received from any person other than police officer. (1 mark each)*
- (b) *Re-write the following sentences after filling-in the blank spaces with appropriate word(s)/figure(s) :*
- (i) *Temporary injunction is granted under order \_\_\_\_\_ of the Code of Civil Procedure, 1908.*
  - (ii) *Declaratory decree is granted under \_\_\_\_\_ of the Specific Relief Act, 1963.*
  - (iii) *A police officer may arrest any person without warrant if he has committed \_\_\_\_\_ offence.*
  - (iv) *\_\_\_\_\_ means any person against whom a decree has been passed or an order capable of execution has been made.*
  - (v) *The law of limitation bars the remedy as well as extinguishes the right where \_\_\_\_\_.*
  - (vi) *A fresh suit is barred for the same cause of action under section(s) \_\_\_\_\_ of the Code of Civil Procedure, 1908.*
  - (vii) *Application for obtaining information with prescribed fees may be submitted to \_\_\_\_\_ officer under the provisions of the Right to Information Act, 2005.*
  - (viii) *Central Information Commission is constituted by \_\_\_\_\_ through a gazette notification. (1 mark each)*

**Answer 6(a)(i)**

(d) 26th January, 1950

**Answer 6(a)(ii)**

(d) Under both (a) and (b)

**Answer 6(a)(iii)**

(d) Both (a) and (b)

**Answer 6(a)(iv)**

(d) Both (b) and (c)

**Answer 6(a)(v)**

(d) Rs.250 per day to the extent of maximum Rs.25,000.

**Answer 6(a)(vi)**

(c) Any sentence except a sentence of death, life imprisonment or imprisonment for a term exceeding seven years.

**Answer 6(a)(vii)**

(b) Rejection of plaint under Order 7, Rule 11 of the Code of Civil Procedure, 1908.

**Answer 6(a)(viii)**

(d) His own knowledge, police report and complaint or information received from any person other than police officer.

**Answer 6(b)**

- (i) Temporary injunction is granted under order **XXXIX** of the Code of Civil Procedure, 1908.
- (ii) Declaratory decree is granted under **Section 34** of the Specific Relief Act, 1963.
- (iii) A police officer may arrest any person without warrant if he has committed **Cognizable** offence.
- (iv) **Judgement debtor** means any person against whom a decree has been passed or an order capable of execution has been made.
- (v) The law of limitation bars the remedy as well as extinguishes the right where **the time limit of recovery of possession of immovable property has elapsed**.
- (vi) A fresh suit is barred for the same cause of action under section(s) **10 and 11** of the Code of Civil Procedure, 1908.
- (vii) Application for obtaining information with prescribed fees may be submitted to **Public Information** officer under the provisions of the Right to Information Act, 2005.
- (viii) Central Information Commission is constituted by **Central Government** through a gazette notification.

**Question 7**

- (a) *Ajit, a Hindu, who has separated from his father Baljit, sells to Charanjit three fields X, Y and Z representing that Ajit is authorised to transfer the same. Of these fields, Field-Z does not belong to Ajit, it having been retained by Baljit on the partition of property. But subsequently on Baljit's death, Ajit, as a heir obtains Field-Z. Decide the validity of the sale of the above said fields in a circumstance where Charanjit does not rescind the contract of sale. (6 marks)*
- (b) *In a case, Hamid was terminated from the police service. Hamid filed a writ petition against termination order on the ground that a reasonable opportunity of being heard was not given to him by the government. The writ petition was dismissed by the court as the government proved that reasonable opportunity of being heard had been given to the petitioner. Afterwards, Hamid filed another writ petition on the ground that as he was appointed by the Director General of Police, termination by the order of Deputy Inspector General of Police was in violation of Article 311(1) of the Constitution of India. Decide the validity of the second writ petition. (5 marks)*
- (c) *Anurag, a child, entered the botanical garden of a municipality and consumed some attractive looking but poisonous berries. As a result of that, he died. The representatives of the child sued the municipality for damages. Will they succeed? Give reasons. (5 marks)*

**Answer 7(a)**

Charanjit may require Ajit to deliver field Z to him. The given problem is an illustration appended to Section 43 of the Transfer of Property Act, 1882, envisaging the doctrine of feeding the grant by estoppel. As per this Section where a grantor has purported to grant an interest in land which he did not at that time possess, but subsequently acquires, the benefit of his subsequent acquisition goes automatically to the earlier grantee or as it usually expressed, feeds the estoppel.

**Answer 7(b)**

The facts of the present problem are similar to the case of *State of U.P. v. Nawab Hussain*, AIR 1977 S.C.1680 pertaining to Section 11 of C.P.C. The Explanation IV to Section 11 of C.P.C. provides that if a plea could have been taken by a party in a proceeding between him and his opponent, he should not be permitted to take that plea against the same party in a subsequent proceeding with reference to the same subject matter.

In the given problem, Hamid should have raised the plea based on violation of Article 311 (1) of the Constitution of India in the first writ petition itself but this was not done. He has raised this issue in the second writ petition which as per Explanation IV, he is not allowed to raise.

**Answer 7(c)**

This problem pertains to the rule of strict or absolute liability stated in the law of torts. This rule of strict/absolute liability has been laid down in *Ryland v. Fletcher* (1868) L.R.3 H.L.330. As per this rule, if any person uses his land in an unnatural way



then he is liable for the wrong committed to any person if such person enters in the land. In the present problem defendant uses his land in unnatural way i.e. municipal garden, by planting such plants having poisonous berries. The child who is unknown about it enters and ate these berries and died. For that, the defendant is liable to pay compensation to the legal representative of the deceased child.

### Question 8

- (a) *On 20th March, Kamal told his wife that he was going to Berhmpore, as Pankaj's wife has written a letter and asked him to come and receive payments due to him. On 21st March, Kamal left his house in time to catch a train for Berhmpore, where Pankaj lived with his wife. On 23rd March, Kamal's dismembered body was found in a box which had been purchased for Pankaj. Decide whether on the trial of Pankaj for the murder of Kamal, the statement made by Kamal to his wife was admissible in evidence. If so, on what grounds ? (6 marks)*
- (b) *Arpit took a debt of Rs. 10,000 from Bharat on January, 1998 and promised to pay by 31st December, 2003. He could not pay such debt within the stipulated time. On 1st December, 2006, Arpit paid Rs. 500 as interest against such debt to Bharat against receipt. Bharat filed a suit against Arpit to recover such debt on 15th December, 2008. Whether the suit filed by Bharat is within the period of limitation ? Decide with reasons citing relevant provisions of the law. (5 marks)*
- (c) *Arjun transfers his property to Bhanu for life and after Bhanu's death to that of his unborn sons as shall first attain the age of 25 years and if no son of Bhanu shall attain that age, to Chandan who is living at the time of the transfer. Decide the validity of this transfer. (5 marks)*

### Answer 8(a)

The facts of the case are similar to that of *Pakala Narayanaswami v. King Emperor*, (1939) LR 66 IA, decided by the Privy Council. In this case the statement was admitted by the Privy Council under Section 32 (1) of the Indian Evidence Act, 1872.

Section 32(1) of the Indian Evidence Act, 1872 dealing with dying declaration states that statements, written or verbal of relevant facts made by a person who is dead are themselves relevant facts in the following case- when the statement is made by a person as to the cause of his death, or as to any of the circumstances of the transaction which resulted in his death, in cases in which the cause of that person's death comes into question.

Such statements are relevant whether the person who made them was or was not, at the time when they were made, under the expectation of the death and whatever may be the nature of the proceeding in which the cause of his death comes into question.

In the present problem the statement made by the deceased (Kamal) to his wife is clearly a statement as to the circumstances of the transaction which resulted in his death. Thus, it is rightly admissible under Section 32(1) of the Indian Evidence Act, 1872. This is so even when the statement has not been made to an independent person.

### Answer 8(b)

The given problem relates to Section 19 of the Limitation Act, 1963. Section 19 provides that where payment on account of a debt or of interest on a legacy is made

before the expiration of the prescribed period by the person liable to pay the debt or legacy or by his agent duly authorized in this behalf, a fresh period of limitation shall be computed from the time when the payment was made.

Provided that, save in the case of payment of interest made before the 1st day of January, 1928, an acknowledgement of the payment appears in the handwriting of, or in a writing signed by, the person making the payment.

In the present problem the limitation period for Bharat to file a suit to recover a debt from Arpit expired on 31st December, 2006. But Arpit paid interest amount on 1st December, 2006 i.e. before the expiry of the limitation period. In view of the provisions of Section 19, Bharat is entitled to a fresh period of limitation of three years from the date of payment of interest by Arpit. Therefore, the suit filed by Bharat on 15th December, 2008 is within the period of limitation.

### **Answer 8(c)**

The present problem is based on Section 14 read with Section 15 and 16 of the Transfer of Property Act, 1882.

Section 14 dealing with the rule against perpetuity contains two propositions, i.e.:

- (1) No transfer is valid after the life-time of one or more persons living at the date of such transfer. Transfer can remain in effect only during the life time of an existing person.
- (2) Transfer can be extended to a person who is not in existence but if he is in existence at the time of termination of the period of last transfer. The moment the person is born he shall have contingent interest and after minority i.e. after the age of 18 years, he shall have vested interest. Barring these two conditions, a restriction on alienation of a property is void.

Section 15 contemplates a situation when a property is transferred and interest is created in favour of a class of persons (and not one individual) some of whom may be or may not be in existence.

In the given case, property is transferred to Bhanu for life and after her death to her unborn sons who shall first attain 25 years of age. Such persons should attain 25 years of age within 18 years of death of Bhanu as under Section 14 vesting cannot be postponed beyond that period.

Therefore, the validity of the transfer can be summarised as follows :

- (1) If Bhanu has any sons, and they will attain the age of 25 years within 18 years of her death, the property will vest with them.
  - (2) If the above condition does not arise, transfer to Chandan is not valid as Section 14 and 15 are violated and as per Section 16, any further transfer is also not valid.
-

**COMPANY ACCOUNTS**  
**COST AND MANAGEMENT ACCOUNTING**

Time allowed : 3 hours

Maximum marks : 100

**NOTE :** All working notes should be shown distinctly.

**PART A**

(Answer Question No. 1 which is compulsory  
and any two of the rest from this part)

**Question 1**

- (a) State, with reasons in brief, whether the following statements are correct or incorrect :
- (i) Accounting Standards (AS) are formulated by International Accounting Standard Board.
  - (ii) A joint stock company cannot purchase its own shares.
  - (iii) If the rate of dividend declared by a company is 22%, then under the Companies (Transfer of Profits to Reserves) Rules, 1975 the percentage of profits to be transferred to reserves should be 10%.
  - (iv) The law limits the commission in case of issue of shares to 10% of the issue price of shares and in case of debentures to 5% or such lower rate as is provided in the articles of association.
  - (v) Contingent liabilities relating to outsiders must be shown on the liability side of the consolidated balance sheet. (2 marks each)
- (b) Re-write the following sentences after filling-in the blank spaces with appropriate word(s)/figure(s) :
- (i) According to the provisions of section 198 of the Companies Act, 1956, maximum limit on the total managerial remuneration payable by public company is \_\_\_\_\_ of net profits.
  - (ii) A company must pay the dividends within \_\_\_\_\_ days of its declaration.
  - (iii) Preliminary expense is a \_\_\_\_\_ asset.
  - (iv) Discount on the issue of debenture is a \_\_\_\_\_ loss.
  - (v) If the purchase price of the debenture includes the interest for the expired period, it is known as \_\_\_\_\_. (1 mark each)
- (c) Gaurav Ltd. had issued 12%, Rs. 10,00,000 debentures @ Rs. 100 each in the past. For the purpose of redemption, it maintains a debenture redemption fund with an annual contribution of Rs. 90,000. On 1st April, 2008, the fund stood at Rs. 4,50,000 represented by 6%, Rs. 5,00,000 government loan.
- On 31st March, 2009, Rs. 2,00,000 government loan was sold @ Rs. 93.50 and the proceeds were utilised to purchase debentures for cancellation @ Rs. 85 each. Assume that Rs. 20,000 debentures have been redeemed out of capital and the balance with face value of Rs. 1,80,000 has been redeemed out of debenture redemption fund account.

*Prepare debenture account, debenture redemption fund account and debenture redemption fund investment account. (5 marks)*

**Answer 1(a)(i)****Incorrect**

Accounting Standards (AS) are formulated by Accounting Standards Board which has been constituted by Council of the Institute of Chartered Accountants of India. The Central Government, in consultation with the National Advisory Committee on Accounting Standards, issues Accounting Standards under Companies (Accounting Standards) Rules, 2006.

**Answer 1(a)(ii)****Incorrect**

Through the introduction of Section 77A in the Companies Act, 1956 by the Companies (Amendment) Act, 1999, the Central Government has allowed the buy-back of its own shares by the companies. The shares can be purchased subject to satisfaction of conditions as provided under Section 77A(2).

**Answer 1(a)(iii)****Correct**

Under the Companies (Transfer of Profit to Reserves) Rules, 1975 as amended, if the rate of dividend is more than 20%, then 10% of profits is to be transferred to reserve.

**Answer 1(a)(iv)****Incorrect**

The law (Companies Act, 1956) limits the commission in case of issue of shares to 5% of the issue price of shares and in case of debentures to 2.5% or such lower rate as is provided in the Articles of Association.

**Answer 1(a)(v)****Incorrect**

Contingent liabilities relating to outsiders are not shown on the liability side of the consolidated balance sheet. It will be shown as contingent liability by way of note/ footnote.

**Answer 1(b)**

- (i) According to the provisions of Section 198 of the Companies Act, maximum limit on the total managerial remuneration payable by public company is **11%** of net profits.
- (ii) A company must pay the dividends within **30 days** of its declaration.
- (iii) Preliminary expense is a **fictitious** asset.
- (iv) Discount on the issue of debenture is a **capital** loss.
- (v) If the purchase price of the debenture includes the interest for the expired period, it is known as **cum-interest purchase/quotation**.

**Answer 1(c)**

<i>Dr.</i>		<b>12% Debentures Account</b>		<i>Cr.</i>	
<i>Date</i>	<i>Particulars</i>	<i>Rs.</i>	<i>Date</i>	<i>Particulars</i>	<i>Rs.</i>
31.3.09	To Debentureholders	1,70,000	1.4.08	By Balance b/d	10,00,000
	To Profit on Redemption of Debentures A/c	30,000			
	To Balance c/d	8,00,000			
		10,00,000			10,00,000
			1.4.09	By Balance b/d	8,00,000

**Debenture Redemption Fund Account**

<i>Date</i>	<i>Particulars</i>	<i>Rs.</i>	<i>Date</i>	<i>Particulars</i>	<i>Rs.</i>
31.3.09	To Capital Reserve (Rs.30,000 + 7,000)	37,000	1.4.08	By Balance b/d	4,50,000
	To General Reserve	1,80,000	31.3.09	By P&L Appropriation A/c	90,000
	To Balance c/d	3,90,000		By Interest on Debenture Redemption Fund Investment (DRFI) A/c (6% of 5,00,000)	30,000
				By DRFI A/c (profit on sale of investment)	7,000
				By Profit on Redemption of Debentures	30,000
		6,07,000			6,07,000

**Debenture Redemption Fund Investment Account**

<i>Date</i>	<i>Particulars</i>	<i>Rs.</i>	<i>Date</i>	<i>Particulars</i>	<i>Rs.</i>
1.4.08	To Balance b/d	4,50,000	31.3.09	By Bank	1,87,000
31.3.09	To Bank	1,20,000		By Balance c/d	3,90,000
	To DR Fund A/c (profit on sale)	7,000			
		5,77,000			5,77,000

*Note* : It is assumed that Rs. 20,000 of debentures have been redeemed out of capital and therefore debentures with face value of Rs. 1,80,000 has been redeemed out of Debenture Redemption Fund Account.

**Question 2**

(a) Write short notes on any two of the following :

(i) Accounting Standard-10 : Accounting for fixed assets

(ii) Issue of shares at a discount

(iii) Taxation on distributed profits. (3 marks each)

(b) Following are the abridged balance sheets of Hary Ltd. and Say Ltd. as on 31st March, 2009 :

Liabilities	Hary Ltd. (Rs.)	Say Ltd. (Rs.)
Equity share capital (Rs. 100 each)	10,00,000	5,00,000
General reserve	1,00,000	1,70,000
Profit and loss account	1,60,000	1,30,000
Current liabilities	4,40,000	2,00,000
	<u>17,00,000</u>	<u>10,00,000</u>
<b>Assets</b>		
Fixed assets	4,80,000	2,50,000
Investment in shares of Say Ltd.	5,00,000	—
Current assets	7,20,000	7,50,000
	<u>17,00,000</u>	<u>10,00,000</u>

Additional information :

(i) On 1st July, 2008, Hary Ltd. acquired 3,000 shares in Say Ltd. The reserves and surplus position of Say Ltd. as on 1st April, 2008 was as under :

General reserve                      Rs. 2,50,000

Profit and loss a/c (Cr.)        Rs. 1,20,000

(ii) On 1st October, 2008, Say Ltd. issued one equity share for every four shares held as bonus shares out of general reserve. No entry has been made in the books of Say Ltd. for issue of bonus shares.

(iii) On 30th September, 2008, Say Ltd. declared a dividend out of pre-acquisition profits @ 25% on Rs.4,00,000, its capital on that date. Hary Ltd. credited the dividend to its profit and loss account.

(iv) Say Ltd. owed Hary Ltd. Rs.50,000 for purchase of stock from Hary Ltd. The entire stock is held by Say Ltd. on 31st March, 2009. Hary Ltd. made a profit of 25% on cost.

Prepare a consolidated balance sheet of Hary Ltd. and its subsidiary Say Ltd. as on 31st March, 2009. (9 marks)

**Answer 2(a)(i)****AS-10 - Accounting for Fixed Assets**

Financial statements disclose information regarding fixed assets such as land and building, plant and machinery, vehicles, furniture and fittings, goodwill, patents, trade marks and designs, etc. The cost of fixed asset should comprise its purchase price and any attributable cost of bringing the asset to its working condition for its intended use. In case of self constructed assets, only direct costs are included in the cost of the asset. In an exchange of assets, the cost of assets given up should be taken as the value of new asset. Fixed asset should be eliminated from the financial statements on disposal or when no further benefit is expected from its use. Losses arising from the retirement or gains or losses arising from disposal of fixed asset which is carried at cost should be recognized in the profit and loss account.

When fixed assets are revalued, an entire class of assets should be revalued or the selection of assets for revaluation should be made on systematic basis. When a fixed asset is revalued upwards, accumulated depreciation existing at the date of revaluation should not be credited to profit and loss account. An increase in net book value arising on revaluation of fixed assets should be credited directly to owner's interest under revaluation reserve. Fixed assets acquired on hire-purchase should be disclosed only at net cash value stating the fact of hire purchase. Where several fixed assets are purchased for a consolidated price, the consideration should be apportioned to various assets on a fair basis as determined by competent valuers. Goodwill should be recorded only when some consideration in money has been paid for it.

The following information should be disclosed in the financial statements :

- (i) Gross and net book values of fixed assets at the beginning and at the end of the accounting period-showing additions, disposals, acquisition etc.
- (ii) Proper disclosure should also be made regarding expenditure incurred in the course of construction or acquisition.
- (iii) Information in respect of revalued assets should include revalued amount substituted for historical cost of fixed assets, the method adopted to compute the revalued amounts, the nature of indices used, the year of any appraisal made and whether an external valuer was involved, etc.

**Answer 2(a)(ii)****Issue of Shares at Discount**

When shares are issued at a price lower than the face value, they are said to be issued at discount. Section 79 of the Companies Act, allows a company to issue shares at a discount subject to the following conditions:

- (i) The shares must belong to a class already issued.
- (ii) The issue is authorised by a resolution passed in the general meeting of the company and the sanction of the Central Government is obtained.
- (iii) The resolution must specify the maximum rate of discount at which the shares

are to be issued. No resolution shall be sanctioned by the Central Government if the maximum rate of discount specified in the resolution exceeds ten per cent, unless it is of opinion that a higher percentage of discount may be allowed in special circumstances of the case.

- (iv) Not less than one year has at the date of the issue elapsed since the date on which the company was entitled to commence business.
- (v) The shares must be issued within two months from the date of receiving the sanctions of the Central Government or within such extended time as the Central Government may allow.

The discount on issue of shares must be treated as a loss of capital nature and debited to a separate account called 'Discount on Issue of Shares Account'. Until it is written off, it must be shown on the assets side of the Balance Sheet under the head "Miscellaneous Expenditure". It is written off gradually out of profits over a reasonable number of years.

### **Answer 2(a)(iii)**

#### **Taxation on Distributed Profits**

The Finance Act, 1997 introduced, an additional income tax, known as tax on distributed profits, on joint stock companies. This tax is designated as tax on distributed profit or dividend distribution tax or corporate dividend tax. Section 115O(1) of the Income-tax Act lays down that any amount declared, distributed or paid by a domestic company by way of dividend, whether interim or otherwise shall be charged tax on distributed profits at specified rates. It is paid in addition to the income tax chargeable on total income. The dividend chargeable to tax on distributed profit may be out of current profits or accumulated profits. The tax on dividend shall be payable even if the company has to pay no tax on profits. Further, it is specified that the tax has to be paid within 14 days from the date of : (a) declaration of dividend, (b) distribution of dividend, or (c) payment of dividend, whichever is earliest. Like rates of income tax, the rate of tax on distributed tax may vary from one financial year to other year.

As tax on distributed profit is levied on the profits distributed, it should be shown below the line i.e. in profit and loss appropriation account. In case of interim dividend, the tax will normally be paid in the same accounting year in which the dividend is declared and paid. In case of proposed dividend, a provision for tax on distributed profit on the amount proposed to be distributed should be made and shown along with the proposed dividend in the profit and loss appropriation account. Thus, tax on distributed profit liability should be disclosed in the profit and loss appropriation account as under:

To Proposed Dividend	XXX
To Tax on Distributed Profit	XXX

In the balance sheet, tax on distributed profit should be shown separately under the head 'Provisions'.



**Answer 2(b)****Consolidated Balance Sheet of Hary Ltd. and its Subsidiary Say Ltd.  
on 31.3. 2009**

<i>Liabilities</i>	<i>Rs.</i>	<i>Assets</i>	<i>Rs</i>
<i>Share Capital</i>			
Equity Share Capital (Rs.10 each)	10,00,000	<i>Fixed Assets :</i>	
Minority Interest	2,00,000	Hary Ltd.	4,80,000
<i>Reserves &amp; Surplus :</i>		S Ltd.	<u>2,50,000</u>
Capital Reserve	1,01,875		7,30,000
General Reserve	1,00,000	<i>Current Assets:</i>	
Profit & Loss Account :		Hary Ltd.	7,20,000
Hary Ltd.	1,60,000	Say Ltd.	<u>7,50,000</u>
<i>Less : Dividend wrongly</i>			<u>14,70,000</u>
credited	75,000	<i>Less : Mutual Owings</i>	<u>50,000</u>
	<u>85,000</u>		14,20,000
<i>Add : H. Ltd's Share in</i>		<i>Less : Unrealised Profit</i>	<u>10,000</u>
Revenue profit of Say Ltd	73,125		14,10,000
	<u>1,58,125</u>		
<i>Less : Unrealised Profit</i>	10,000		
<i>Current Liabilities :</i>	1,48,125		
Hary Ltd.	4,40,000		
Say Ltd.	<u>2,00,000</u>		
	6,40,000		
<i>Less : Mutual Owing</i>	<u>50,000</u>		
	5,90,000		
	<u>21,40,000</u>		<u>21,40,000</u>

**Working Notes :****(i) Capital Profits (Pre-acquisition profits)**

	<i>Rs.</i>	<i>Rs.</i>
General Reserve (1.4.2008)	2,50,000	
<i>Less : Bonus issue</i>	<u>1,00,000</u>	
Pre-acquisition Reserve		1,50,000
Profit & Loss A/c (1.4.2008)	1,20,000	
<i>Less : Dividend out of pre-acquisitions profit</i> <i>(25% on Rs.4,00,000)</i>	<u>1,00,000</u>	20,000
Profit of Current Year (pre-acquisition) (1.4.2008 to 30.6.2008)		<u>32,500</u>
		<u>2,02,500</u>
Hary Ltd.'s share (75%)		1,51,875
Minority Interest		<u>50,625</u>

<b>(ii) Revenue Profits (1.7.2008 to 31.3.2009)</b>	<i>Rs.</i>
Profit & Loss A/c as on 31.3.2009	1,30,000
Less : Opening Balance (1,20,000 – 1,00,000)	<u>20,000</u>
	1,10,000
Add : Transfer to Reserve (Rs.1,70,000 – 1,50,000)	<u>20,000</u>
Profits earned during the year	<u>1,30,000</u>
Profit for the pre-acquisition period (Rs.1,30,000 x 3/12)	32,500
Profit for the post-acquisition period (Rs.1,30,000 x 9/12)	<u>97,500</u>
Hary Ltd. Share (3/4)	73,125
Minority Interest	<u>24,375</u>

**(iii) Calculation of Capital Reserve**

	<i>Rs.</i>
Paid up capital	3,00,000
Share of bonus shares	75,000
Share of capital profit	<u>1,51,875</u>
	5,26,875
Less : Cost of Investment	5,00,000
Less : Dividend out of capital profit credited to Profit & Loss Account	<u>75,000</u>
Capital Reserve	<u>1,01,875</u>

**(iv) Minority Interest**

Share Capital	1,00,000
Share of bonus shares	25,000
Share of capital profits	50,625
Share of revenue profits	<u>24,375</u>
	<u>2,00,000</u>

**Question 3**

(a) Abridged balance sheet of Rama Ltd. as on 31st March, 2009 is as follows :

<i>Liabilities</i>	<i>Rs.</i>
Share capital	6,00,000
Reserves and surplus	50,000
Bank overdraft	10,000
Creditors	60,000
Provision for taxation	1,10,000
Proposed dividend	<u>60,000</u>
	<u>8,90,000</u>

<b>Assets</b>	
Fixed assets	3,70,000
Current assets	5,20,000
	<u>8,90,000</u>

The net profits of the company after deducting working expenses but before providing for taxation were as under :

Year	Rs.
2006-07	3,18,000
2007-08	3,40,000
2008-09	3,12,000

On 31st March, 2009, fixed assets were at Rs.4,50,000. Sundry debtors on the same date included Rs.10,000 which is irrecoverable. Having regard to the type of business, a 10% return on average capital employed is considered as reasonable. Ascertain the value of goodwill on the basis of three years purchase of annual super profits. Also calculate goodwill by capitalisation of average maintainable profits. Depreciation on fixed assets is charged @ 10% per annum and the rate of tax is 30%. (6 marks)

(b) Following is the profit and loss account of Azad Ltd. for the year ended 31st March, 2009 :

	Rs.
To Office and administrative expenses	3,10,000
To Selling and distribution expenses	1,92,000
To Directors' fees	39,500
To Managerial remuneration	1,70,000
To Interest on debentures	18,500
To Donation to charitable trust	15,000
To Compensation for breach of contract	27,000
To Depreciation on fixed assets	3,12,000
To Investment revaluation reserve	12,500
To Provision for taxation	7,40,000
To General reserve	2,50,000
To Balance c/d	8,46,500
	<u>29,33,000</u>
By Balance b/d	3,43,200
By Gross profit b/d	24,15,000
By Subsidies	1,39,300
By Interest on investment	9,500
By Transfer fees	1,000
By Profit on sale of machinery (W.D.V. Rs.30,000)	25,000
	<u>29,33,000</u>

*Additional information :*

- *Original cost of the machinery sold was Rs.40,000.*
- *Depreciation on fixed assets as per Schedule XIV of the Companies Act, 1956 was Rs. 3,42,000.*

*You are required to calculate managerial remuneration in the following situations:*

- (i) when there is only whole-time director;*
  - (ii) when there are two whole-time directors; and*
  - (iii) when there are two whole-time directors, a managing director and a part-time director. (6 marks)*
- (c) Differentiate between 'shares' and 'debentures'. (3 marks)*

### **Answer 3(a)**

#### **Calculation of Average Capital Employed**

		<i>Rs.</i>
Fixed Assets		4,50,000
Current Assets Rs.(5,20,000 – 10,000)		<u>5,10,000</u>
	<i>Rs.</i>	9,60,000
<i>Less : Bank overdraft</i>	10,000	
<i>Creditors</i>	60,000	
Provision for taxation	<u>1,10,000</u>	<u>1,80,000</u>
Capital employed		7,80,000
<i>Less : Half of the profit after tax of the current year</i>		<u>1,09,200</u>
Average capital employed		<u>6,70,800</u>

#### **Calculation of Average Adjusted Profits**

Total profits for last 3 years		9,70,000
<i>Less : Provision for bad debts</i>		10,000
		<u>9,60,000</u>
Average Profit		3,20,000
<i>Less : Depreciation on revaluation of fixed assets 10%</i>		
Rs. (4,50,000 – 3,70,000)		<u>(8,000)</u>
		3,12,000
<i>Less : Income Tax @ 30%</i>		<u>(93,600)</u>
Average maintainable profit		2,18,400
<i>Less : Normal Profit 10% of 6,70,800</i>		<u>(67,080)</u>
Super Profit		<u>1,51,320</u>

Goodwill at 3 years purchase = Super profit x No. of years

$$= \text{Rs.}1,51,320 \times 3 = \text{Rs.} 4,53,960$$

Goodwill as per Capitalization Method = Capitalized value – Actual capital employed

Capitalized value = (Average maintainable profit x 100) / Normal rate of profit

= Rs. (2,18,400 x 100) / 10

= Rs. 21,84,000

Goodwill = Rs. 21,84,000 – Rs. 7,80,000 = Rs. 14,04,000

**Answer 3(b)**

	<i>Rs.</i>	<i>Rs.</i>
Gross profit as per Profit & Loss Account		24,15,000
<i>Add</i> : Subsidies	1,39,300	
Interest on investments	9,500	
Transfer fees	1,000	
Profit on sale of machinery (Cost – W.D.V.) (40,000 – 30,000)	10,000	<u>1,59,800</u>
		25,74,800
<i>Less</i> : Office and administrative expenses	3,10,000	
Director's fees	39,500	
Selling and distribution expenses	1,92,000	
Interest on debentures	18,500	
Compensation for breach of contract	27,000	
Depreciation as per Schedule XIV	<u>3,42,000</u>	<u>9,29,000</u>
		<u>16,45,800</u>

**Computation of managerial remuneration :**

- (i) When there is only one whole-time director :  
5% of Rs.16,45,800 Rs. 82,290
- (ii) When there are two whole-time directors :  
10% of Rs.16,45,800 Rs. 1,64,580
- (iii) When there are two whole-time directors, a  
managing director and a part-time director:  
11% of Rs.16,45,800 Rs. 1,81,038

**Answer 3(c)**

The following are the points of difference between shares and debentures :

- (i) A person holding the shares is the part-owner of the company but a person holding the debentures is the creditor of the company.
- (ii) Voting and other rights are available to shareholders and not to debenture- holders.
- (iii) Dividend is paid on shares but on debentures, interest is paid.
- (iv) A debenture holder is certain of return on his investment while a shareholder

cannot get dividend if the company does not earn profits, even if there are profits, the company does not declare a dividend.

- (v) No security is provided for shares but debentures may be secured.
- (vi) In the case of winding-up of a company, the amount of debentures will be repaid before any amount is paid to shareholders to return share capital.
- (vii) For issue of shares at a discount, certain conditions as specified in Section 79 of the Companies Act are to be satisfied but there is no restriction for issue of debentures at a discount.
- (viii) Debentures can be converted into shares but shares cannot be converted into debentures.

#### Question 4

(a) *Jolly Ltd. has the following balance sheet as on 31st March, 2008 :*

<i>Liabilities</i>	<i>Rs.</i>
<i>Share capital :</i>	
<i>Issued, subscribed and fully paid-up (10,000 equity shares of Rs. 100 each)</i>	<i>10,00,000</i>
<i>5,000 Preference shares of Rs. 100 each</i>	<i>5,00,000</i>
<i>Capital reserve</i>	<i>1,00,000</i>
<i>Securities premium account</i>	<i>1,00,000</i>
<i>General reserve</i>	<i>2,00,000</i>
<i>Profit and loss account</i>	<i>1,00,000</i>
<i>Current liabilities</i>	<i>10,00,000</i>
	<u><u><i>30,00,000</i></u></u>
 <i>Assets</i>	
<i>Fixed assets</i>	<i>22,00,000</i>
<i>Current assets</i>	<i>8,00,000</i>
	<u><u><i>30,00,000</i></u></u>

*The preference shares are to be redeemed at 10% premium. Fresh issue of equity shares is to be made to the extent it is required under the Companies Act, 1956 for the purpose of this redemption. The shortfall in funds for the purpose of the redemption after utilising the proceeds of the fresh issue are to be met by taking a bank loan. Show journal entries. (6 marks)*

(b) *Silver Ore Co. Ltd. was formed on 1st April, 2007 with an authorised capital of*

*Rs.6,00,000 in shares of Rs.10 each. Of these, 52,000 shares had been issued and subscribed but there were calls-in-arrears on 100 shares. From the following trial balance as on 31st March, 2008, prepare the trading and profit and loss account and the balance sheet :*

	Rs.	Rs.
Cash at bank	1,05,500	—
Share capital	—	5,19,750
Plant	40,000	—
Sale of silver	—	1,79,500
Mines	2,20,000	—
Promotional expenses	6,000	—
Interest on fixed deposit upto 31st December	—	3,900
Dividend on investment less 22% tax	—	3,200
Royalties paid	10,000	—
Railway track and wagons	17,000	—
Wages of miners	74,220	—
Advertising	5,000	—
Carriage on plant	1,800	—
Furniture and buildings	20,900	—
Administrative expenses	28,000	—
Repairs	900	—
Coal and oil	6,500	—
Cash	530	—
Investments in shares of Tin Mines	80,000	—
Brokerage on Tin Mines	1,000	—
6% Fixed deposit in Syndicate Bank	89,000	—
	<u>7,06,350</u>	<u>7,06,350</u>

*Depreciate plant and railway track and wagons by 10%, furniture and building by 5%. Write off one-third of the promotional expenses. Value of silver on 31st March, 2008 was Rs. 15,000. On 10th December, 2007, the directors forfeited 100 shares of which only Rs.7.50 per share had been paid. Ignore corporate dividend tax.*

*(9 marks)*

**Answer 4(a)****Journal Entries in the Books of Jolly Ltd.**

<i>Particulars</i>	<i>Dr. (Rs.)</i>	<i>Cr. (Rs.)</i>
Securities Premium A/c	Dr. 50,000	
To Premium on Redemption of Preference Shares Account		50,000
(Utilization of securities premium on Redemption of Preference Shares)		
General Reserve	Dr. 2,00,000	
Profit & Loss Account	Dr. 1,00,000	
To Capital Redemption Reserve A/c		3,00,000
(Creation of Capital Redemption Reserve to the maximum possible extent)		
Bank	Dr. 2,00,000	
To Equity Share Application and Allotment A/c		2,00,000
(Receipt of money for equity shares of Rs.2,00,000)		
Equity Share Application and Allotment Account	Dr. 2,00,000	
To Equity Share Capital Account		2,00,000
(Allotment of equity shares of the face value of Rs. 2,00,000 at par)		
Preference Share Capital Account	Dr. 5,00,000	
Premium on Redemption of Preference Shares A/c	Dr. 50,000	
To Sundry Preference Shareholders A/c		5,50,000
(Amount payable to sundry preference shareholders to redeem 5,000 preference shares of Rs.100 each at a premium of Rs.10 per share)		
Bank	Dr. 3,50,000	
To Bank Loan Account		3,50,000
(Raising a bank loan to pay off the amount due to sundry preference shareholders)		
Sundry Preference Shareholders Account	Dr. 5,50,000	
To Bank		5,50,000
(Payment made to sundry preference shareholders)		



**Answer 4(b)**

**Silver Ore Ltd.**  
**Trading and Profit & Loss A/c**  
*(For the year ending March 31, 2008)*

<i>Particulars</i>	<i>Rs.</i>	<i>Particulars</i>	<i>Rs.</i>
To Royalties	10,000	By Sales	1,79,500
To Wages of Mines	74,220	By Stock of Silver	15,000
To Coal and Oil	6,500		
To Depreciation on Plant	4,180*		
To Depreciation on Railway Track and Wagons	1,700		
To Gross Profit	97,900		
	<u>1,94,500</u>		<u>1,94,500</u>
To Administrative Expenses	28,000	By Gross Profit	97,900
To Promotion Expenses	2,000	By Interest on F.D. 3,900	
To Advertising	5,000	Add : Accrued 1,440	5,340
To Depreciation on Furniture and Building	1,045	By Dividend on Investments (Grossed = 100/78 x 3,200)	4,103
To Repairs	900		
To Net Profit carried to Balance Sheet	70,398		
	<u>1,07,343</u>		<u>1,07,343</u>

*NOTE : \*Carriage on plant has been added to the cost of plant and depreciation is charged accordingly.*

**Balance Sheet of Silver Ore Ltd.**  
*(As on March 31, 2008)*

<i>Liabilities</i>	<i>Rs.</i>	<i>Assets</i>	<i>Rs.</i>
<i>Share Capital :</i>		<i>Fixed Assets :</i>	
Authorised Capital		Mines	2,20,000
60,000 shares of Rs.10 each	6,00,000	Railway Track and Wagons 17,000	
Issued Capital :	<u>        </u>	Less : Depreciation 1,700	15,300
52,000 Shares of Rs.10 each	5,20,000	Plant 41,800	
Subscribed Capital :	<u>        </u>	Less : Depreciation 4,180	37,620
51,900 shares of Rs.10 each	5,19,000	Building and Furniture 20,900	
fully paid		Less : Depreciation 1,045	19,855
Add : Share forfeited account (100 x 7.50)	750	<i>Investment at cost :</i>	
	<u>5,19,750</u>	Shares of Tin Mines	81,000
<i>Reserves and Surplus :</i>		<i>Current Assets :</i>	
Profit and Loss Account	70,398	Stock of Silver Ore	15,000
		Cash at Bank	1,05,500
		Cash in hand	530
		Accrued Interest	1,440

<i>Liabilities</i>	<i>Rs.</i>	<i>Assets</i>	<i>Rs.</i>	<i>Rs.</i>
		<i>Loans and Advance :</i>		
		Fixed Deposit		89,000
		Tax Deducted at Source		903
		<i>Miscellaneous Expenditure :</i>		
		Promotion Expenses		4,000
	<u>5,90,148</u>			<u>5,90,148</u>

**PART B**

*(Answer Question No. 5 which is compulsory  
and any two of the rest from this part.)*

**Question 5**

(a) *State, with reasons in brief, whether the following statements are true or false :*

- (i) *At break-even point, the company earns only marginal profit.*
- (ii) *Fixed cost per unit remains fixed.*
- (iii) *Liquidity ratios measure long-term solvency of a concern.*
- (iv) *Rent on owned building is included in cost accounts.*
- (v) *Job costing can be used in industries using standard costing.*

*(2 marks each)*

(b) *Re-write the following sentences after filling-in the blank spaces with appropriate word(s)/figure(s) :*

- (i) *Inflated price method of valuing material issue is suited when \_\_\_\_\_.*
- (ii) *Abnormal wastage \_\_\_\_\_ part of cost of production.*
- (iii) *\_\_\_\_\_ in a contract provides that the contract price would be suitably enhanced on the happening of a specified contingency.*
- (iv) *Direct material + direct labour + factory overheads = \_\_\_\_\_.*

*(1 mark each)*

(c) *Distinguish between any two of the following :*

- (i) *'Bin card' and 'stores ledger'.*
- (ii) *'Fixed cost' and 'variable cost'.*
- (iii) *'Absorption costing' and 'marginal costing'.*

*(3 marks each)*

**Answer 5(a)(i)**

**False.**

Break-even point is a point of no profit and no loss, i.e. it is the quantity or amount of sales where there is neither profit nor loss. At this point, contribution will be equal to fixed cost.

**Answer 5(a)(ii)**

**False.**

It is the total fixed cost which remains fixed irrespective of the level of output. But

the fixed cost per unit will be different at different level of output. As level of output increases the fixed cost per unit will decrease and *vice-versa*.

**Answer 5(a)(iii)**

**False.**

Liquidity ratios measure the short term solvency of a concern. These ratios indicate the relationship between current assets/liquid assets and the current liabilities of the concern.

**Answer 5(a)(iv)**

**True.**

Rent on owned building is included in cost accounts, it is done to calculate the real cost after taking into account the notional rent which would have been paid, had the building been taken on rent.

**Answer 5(a)(v)**

**True.**

Job costing can be used in industries using standard costing, since standard costing is a technique which can be used with any methods of costing including job costing.

**Answer 5(b)**

- (i) Inflated price method of valuing material issue is suited when there **is unavoidable wastage of material.**
- (ii) Abnormal wastage **is not** part of cost of production.
- (iii) **Escalation clause** in a contract provides that the contract price would be suitably enhanced on the happening of a specified contingency.
- (iv) Direct material + Direct Labour + Factory overheads = **Factory Cost /Works Cost.**

**Answer 5(c)(i)**

**Bin Card and Stores Ledger**

Following are the distinction between bin card and stores ledger :

<i>Bin Card</i>	<i>Stores Ledger</i>
1. It is a record of quantity	It is a record of quantity and value.
2. It is kept inside the stores.	It is kept outside the stores.
3. It is maintained by the store keeper.	It is maintained by the accounts department.
4. The postings are done before the transactions take place.	The postings are done after the transactions take place.
5. Each transaction is individually posted.	Transactions may be posted periodically and in total.

**Answer 5(c)(ii)**

Following are the points of distinction between fixed cost and variable cost :

1. Fixed cost is the cost which does not vary but remains constant within a given period of time and range of activity in spite of the fluctuations in production. Variable cost is the cost which varies directly in proportion to every increase or decrease in the volume of output of production. Fixed costs are sometimes referred to as “period costs” while variable costs as “product costs” in system of direct costing.
2. The variable cost per unit output remains the same while fixed cost per unit changes as the output increases or decreases and fixed cost remains constant in total.

**Answer 5(c)(iii)**

Following are the main distinctions between absorption costing and marginal costing:

<i>Absorption costing</i>	<i>Marginal costing</i>
(i) Fixed production overheads are charged to the product to be subsequently released as a part of goods sold i.e., it is included in cost per unit.	Fixed production costs are regarded as period cost and are charged to revenue along with the selling and administration expenses, i.e., they are not included while computing cost per unit.
(ii) Profit is the difference between sales and cost of goods sold.	Profit in marginal costing is ascertained by establishing the total contribution and then deducting there from the total fixed expenses. Contribution is the excess of sales over variable cost.
(iii) Costs are seldom classified into variable and fixed. Although such a classification is possible, it fails to establish a cost-volume profit relationship.	Cost-volume profit relationship is an integral part of marginal costing. Costs have to be classified into fixed costs and variable costs.
(iv) If inventories increase during a period, this method will reveal more profit than marginal costing. When inventories decrease, less profit are reported because under this method closing stock is valued at higher figures. Since inventories are valued at total cost, a portion of fixed overheads are also included in inventories.	If inventories increase during a period, this method generally reports less income than absorption costing; but when inventories decrease this method reports more net income. The difference in the net income is due to difference in accounting for fixed manufacturing costs as compared to inventory valuation.

<i>Absorption costing</i>	<i>Marginal costing</i>
(v) Arbitrary apportionment of fixed costs may result in under or over recovery of overheads.	Since fixed costs are excluded, there is no question of arbitrary apportionment of fixed overheads and thus no under or over absorption of overheads.

**Question 6**

(a) A company has provided you the following details :

<i>Liabilities</i>	<i>31.12.2007</i>	<i>31.12.2008</i>
	<i>(Rs.)</i>	<i>(Rs.)</i>
<i>Share capital</i>	<i>70,000</i>	<i>74,000</i>
<i>Debentures</i>	<i>12,000</i>	<i>6,000</i>
<i>Reserve for doubtful debts</i>	<i>700</i>	<i>800</i>
<i>Trade creditors</i>	<i>10,360</i>	<i>11,840</i>
<i>Profit and loss a/c</i>	<i>10,040</i>	<i>10,560</i>
	<u><i>1,03,100</i></u>	<u><i>1,03,200</i></u>
 <i>Assets</i>		
 <i>Cash</i>	 <i>9,000</i>	 <i>7,800</i>
<i>Debtors</i>	<i>14,900</i>	<i>17,700</i>
<i>Stock</i>	<i>49,200</i>	<i>42,700</i>
<i>Land</i>	<i>20,000</i>	<i>30,000</i>
<i>Goodwill</i>	<i>10,000</i>	<i>5,000</i>
	<u><i>1,03,100</i></u>	<u><i>1,03,200</i></u>

*Additional information —*

— *Dividend paid Rs.3,500; and*

— *Land was purchased for Rs.10,000.*

*Prepare a cash flow statement as per Accounting Standard-3 (Revised).*

*(6 marks)*

(b) *Lookahead Ltd. produces and sells a single product. Sales budget for the calendar year 2009 for each quarter is as under :*

<i>Quarter</i>	<i>No. of Units to be Sold</i>
<i>I</i>	<i>12,000</i>
<i>II</i>	<i>15,000</i>
<i>III</i>	<i>16,500</i>
<i>IV</i>	<i>18,000</i>

The year 2009 is expected to open with an inventory of 4,000 units of finished product and close with an inventory of 6,500 units.

Production is customarily scheduled to provide for two-thirds of the current quarter's demand plus one-third of the following quarter's demand. Thus production anticipates sales volume by about one month. The standard cost details for one unit of the product is as follows :

- Direct materials 10 Kgs. @ 50 paise per kg.
- Direct labour 1 hour 30 minutes @ Rs.4 per hour.
- Variable overheads 1 hour 30 minutes @ Re.1 per hour.
- Fixed overheads 1 hour 30 minutes @ Rs.2 per hour based on a budgeted production volume of 90,000 direct labour hours for the year.

Answer the following —

- (i) Prepare a production budget for the year 2009 by quarters, showing the number of units to be produced. (3 marks)
- (ii) If the budgeted selling price per unit is Rs.17, what would be the budgeted profit for the year as a whole ? (3 marks)
- (iii) In which quarter of the year the company is expected to break-even ? (3 marks)

**Answer 6(a)**

**Cash Flow Statement of .....**  
**for the year ended 31st December, 2008**

	Rs.	Rs.
<b>(A) Cash Flow from Operating Activities :</b>		
Increase in balance of Profit & Loss A/c	520	
Adjustments for non-cash and non-operating items :		
Reserve for doubtful debts	100	
Dividend	3,500	
Goodwill written off	5,000	
Operating profits before working capital changes	9,120	
Adjustments for changes in current assets and liabilities :		
Increase in trade creditors	1,480	
Increase in debtors	(2,800)	
Decrease in stock	6,500	
Cash generated from operations	14,300	
Income-tax paid	—	
Net cash from operating activities		14,300

	<i>Rs.</i>	<i>Rs.</i>
<b>(B) Cash Flow from Investing Activities :</b>		
Purchase of Land	(10,000)	
Net cash used in investing activities		(10,000)
<b>(C) Cash Flow from Financing Activities :</b>		
Proceeds from issue of share capital	4,000	
Redemption of Debentures	(6,000)	
Dividend paid	(3,500)	
Net cash used in financing activities		<u>(5,500)</u>
Net decrease in cash and cash equivalents [ (A) + (B) + (C) ]		(1,200)
Cash and cash equivalents at the beginning of the period		<u>9,000</u>
Cash and cash equivalents at the end of the period		<u>7,800</u>

**Answer 6(b)**

Number of units to be sold during the year 2009

Quarter I	12,000 units
Quarter II	15,000 units
Quarter III	16,500 units
Quarter IV	18,000 units
Sales during the year	<u>61,500 units</u>

**(i) Production Budget (for the year 2009 by quarters)**

	<i>Quarter I Units</i>	<i>Quarter II Units</i>	<i>Quarter III Units</i>	<i>Quarter IV Units</i>	<i>Total Units</i>
Units to be produced in each quarter : 2/3rd of the current quarter's sales demand	8,000 (2/3 x 12,000)	10,000 (2/3 x 15,000)	11,000 (2/3 x 16,500)	12,000 (2/3 x 18,000)	41,000
<i>Add</i> : 1/3 of the following quarter's sales demand in first 3 quarters and closing inventory in the 4th quarter	5,000 (1/3 x 15,000)	5,500 (1/3 x 16,500)	6,000 (1/3 x 18,000)	6,500	23,000
<b>Total</b>	<b>13,000</b>	<b>15,500</b>	<b>17,000</b>	<b>18,500</b>	<b>64,000</b>

## (1) Variable Cost per unit

		<i>Rs.</i>	<i>Rs.</i>
Direct Material	: 10 kgs. @ 50 paise per kg.	5.00	
Direct labour	: 1-½ hours @ Rs.4 per hour	6.00	
Variable overheads	: 1-½ hours @ Re.1 per hour	<u>1.50</u>	12.50

(2) Fixed overhead per annum : 90,000 hrs. @ Rs. 2 = Rs.1,80,000

(ii) **Statement of Budgeted Profit for the year (as a whole)**

	<i>Rs.</i>
Total Sales : 61,500 units @ Rs.17 per unit	10,45,000
Less : Total Variable Cost : 61,500 units @ 12.50 per unit	<u>7,68,750</u>
Contribution	2,76,750
Less : Fixed cost for the year	<u>1,80,000</u>
Profit for the year 2009 as a whole	<u>96,750</u>

(iii) **Calculation of Break-even point/sales**

$$\begin{aligned} \text{Break Even Point} &= \frac{\text{Fixed Overheads}}{\text{Selling Price per unit} - \text{Variable Cost per unit}} \\ &= \frac{\text{Rs. 1,80,000}}{(\text{Rs. 17} - \text{Rs. 12.50})} = 40,000 \text{ units.} \end{aligned}$$

Total sales (in units) by the end of 3rd quarter will be 43,500 (i.e. 12,000 + 15,000 + 16,500).

Therefore, the company will break-even in the later part of the 3rd quarter.

**Question 7**(a) *Material-A is used as follows :*

- Minimum usage* – 500 units per week
  - Maximum usage* – 1,500 units per week
  - Normal usage* – 1,000 units per week
  - Ordering quantities* – 1,600 units
  - Delivery period* – 4-6 weeks
- Calculate —*

- (i) *Maximum level.* (2 marks)
- (ii) *Minimum level.* (2 marks)
- (iii) *Ordering level.* (2 marks)



- (b) On 1st July, 2007, Delux Ltd. undertook a contract for Rs.5,00,000. On 30<sup>th</sup> June, 2008 when the accounts were closed, the following details about the contract were gathered :

	Rs.
Material purchased	1,00,000
Wages paid	45,000
General expenses	10,000
Plant purchased	50,000
Materials on hand (30.6.2007)	25,000
Wages accrued (30.6.2008)	5,000
Work certified	2,00,000
Cash received	1,50,000
Work uncertified	15,000
Depreciation of plant	5,000

The above contract has an escalation clause which reads as follows :

*“In the event of prices of materials and rates of wages increase by more than 5%, the contract price would be increased accordingly by 25% of the rise in the cost of materials and wages beyond 5% in each case.”*

*It was found that since the date of signing the agreement, the prices of materials and wage rates increased by 25%. The value of the work certified does not take into account the effect of the above clause.*

Prepare the contract account. (6 marks)

- (c) Differentiate between ‘Halsey wage plan’ and ‘Rowan wage plan’. (3 marks)

**Answer 7(a)**

$$\begin{aligned}
 \text{Ordering level} &= \text{Maximum usage} \times \text{Maximum delivery period} \\
 &= 1,500 \times 6 = 9,000 \text{ units} \\
 \text{Minimum level} &= \text{Ordering level} - (\text{Normal usage} \times \text{Normal delivery period}) \\
 &= 9,000 - (1,000 \times 5) \\
 &= 9,000 - 5,000 = 4,000 \text{ units} \\
 \text{Minimum level} &= (\text{Ordering level} + \text{Ordering Quantity}) - (\text{Minimum usage} \times \\
 &\quad \text{Minimum delivery period}) \\
 &= (9,000 + 1,600) - (500 \times 4) \\
 &= 10,600 - 2,000 = 8,600 \text{ units}
 \end{aligned}$$

**Answer 7(b)****Contract Account**

Dr. For the year ending 30th June, 2008 Cr.

Particulars	Rs.	Particulars	Rs.
To Materials	1,00,000	By Work-in-Progress :	
To Wages (Rs.45,000 + Rs.5,000)	50,000	Work certified	2,00,000
To General Expenses	10,000	Work uncertified	15,000
To Depreciation of Plant	5,000	By Materials on hand	25,000
To Notional Profit c/d	80,000	By Contract Escalation(1)	5,000
	2,45,000		2,45,000
To Profit and Loss A/c		By Notional Profit b/d	80,000
$\left[ \text{Rs. } 80,000 \times \frac{1}{3} \times \frac{\text{Rs. } 1,50,000}{\text{Rs. } 2,00,000} \right]$	20,000		
To Work-in-Progress A/c(Reserve)	60,000		
	80,000		80,000

*Working Note (1)*

Particulars	Total increase Rs.	Upto 5% Rs.	Beyond 5% Rs.
Materials			
(Rs.1,00,000 – Rs.25,000) x $\frac{25}{125}$			
[in the ratio of 5:20 ]	15,000	3,000	12,000
Wages Rs. 50,000 x $\frac{25}{125}$	10,000	2,000	8,000
Total Increase	25,000	5,000	20,000

Increase in contract price = 25% of increase in material and wages beyond 5%

$$= \frac{25}{100} \times \text{Rs. } 20,000 = \text{Rs. } 5,000$$

**Answer 7(c)**

Total wages under Halsey Wage Plan and Rowan Wage Plan is calculated as under:

*Halsey Plan :*

Total Wages = Time taken x Hourly rate +  $\frac{1}{2}$  (Time saved) x Hourly rate

*Rowan Plan*

$$\text{Total Wages} = \text{Time taken} \times \text{Hourly rate} + \left[ \frac{\text{Time saved}}{\text{Standard time}} \right] \times \text{Time taken} \times \text{Hourly Rate}$$

The following are the points distinction between Halsey wage plan and Rowan wage plan:

- (i) In Halsey wage plan bonus is usually set at 50% of the time saved and it does not serve as strong incentive, whereas under Rowan wage plan bonus is that portion of the wages of the time taken which time saved bears to the standard time, and serves as a strong incentive for increasing efficiency.
- (ii) In Rowan wage plan the quality of work does not suffer much as the worker is not induced to rush through the work since bonus increases at a decreasing rate at higher levels of efficiency. In Halsey wage plan, the worker is induced to rush through the work since he gets extra wages for every 50% of the time saved.
- (iii) The effective labour rate per hour in Rowan wage plan is higher up to 50% of the time saved and falls thereafter whereas in the Halsey wage plan the effective labour rate per hour is lower up to 50% of the time saved.
- (iv) If the time taken is more than the time saved, then worker is benefitted under Rowan Plan, while in case time saved is more, workers are benefitted under Halsey Plan.

**Question 8**

From the following information, prepare the projected trading and profit and loss account for the next financial year ending 31st March, 2009 and the projected balance sheet as on that date :

<i>Gross profit ratio</i>	<i>25%</i>
<i>Net profit to equity capital</i>	<i>10%</i>
<i>Stock turnover ratio</i>	<i>5 times</i>
<i>Average debt collection period</i>	<i>2 months</i>
<i>Creditors velocity</i>	<i>3 months</i>
<i>Current ratio</i>	<i>2</i>
<i>Proprietary ratio (Fixed assets to capital employed)</i>	<i>80%</i>
<i>Capital gearing ratio (Preference shares and debentures to total long-term funds)</i>	<i>30%</i>
<i>General reserve and profit and loss to equity shareholders' fund</i>	<i>20%</i>
<i>Preference share capital to debentures</i>	<i>2</i>

Cost of sales consists of 40% for materials and balance for wages and overheads.  
Gross profit is Rs. 6,00,000. (15 marks)

**Answer 8****Projected Trading and Profit & Loss Account for the year ending March 31, 2009**

<i>Dr.</i>		<i>Cr.</i>	
<i>Particulars</i>	<i>Rs.</i>	<i>Particulars</i>	<i>Rs.</i>
To Material used	7,20,000	By Sales	24,00,000
To Wages and overheads	10,80,000		
To Gross profit c/d	6,00,000		
	<u>24,00,000</u>		<u>24,00,000</u>
To Expenses (Balancing figure)	4,93,600	By Gross profit b/d	6,00,000
To Net profit	1,06,400		
	<u>6,00,000</u>		<u>6,00,000</u>

**Projected Balance Sheet as on March 31, 2009**

<i>Liabilities</i>	<i>Rs.</i>	<i>Assets</i>	<i>Rs.</i>
Share Capital :		Fixed Assets	15,20,000
Equity Share Capital	10,64,000	Current Assets :	
Preference Share Capital	3,80,000	Stock	3,60,000
Reserves and Surplus :		Debtors	4,00,000
General Reserve	1,59,600		
Profit & Loss Account	1,06,400		
Secured Loans :			
Debentures	1,90,000		
Current Liabilities :			
Trade Creditors	1,80,000		
Bank Overdraft	2,00,000		
	<u>22,80,000</u>		<u>22,80,000</u>

**Working Notes :**

- Rs.
- (i) Gross Profit 6,00,000  
Gross Profit being 25% of sales  
Sales = Rs. 6,00,000 x 100/25 = Rs. 24,00,000
- (ii) Cost of Sales = Sales – Gross profit  
= Rs. 24,00,000 – Rs. 6,00,000 = Rs. 18,00,000

- (iii) Material used = 40% of Cost of sales  
 $= 40/100 \times \text{Rs. } 18,00,000 = \text{Rs. } 7,20,000$
- (iv) Wages and overheads = Rs. 18,00,000 – Rs. 7,20,000 = Rs. 10,80,000
- (v) Stock = Cost of sales / Stock turnover ratio = Rs. 18,00,000/5 = Rs. 3,60,000
- (vi) Debtors = Sales for 2 months = Rs. 24,00,000 x 2/12 = Rs. 4,00,000
- (vii) As current ratio is 2, Current liabilities are half of current assets  
 Hence, current liabilities =  $\frac{1}{2} \times (\text{Rs. } 3,60,000 + \text{Rs. } 4,00,000) = \text{Rs. } 3,80,000$
- (viii) Trade Creditors = 3 months of material consumed  
 $= \text{Rs. } 7,20,000 \times 3/12 = \text{Rs. } 1,80,000$
- (ix) Bank overdraft = Rs. 3,80,000 – 1,80,000 = Rs. 2,00,000
- (x) Fixed assets to capital employed = 80%  
 Hence, working capital to capital employed = 20%  
 Working Capital = Current assets – Current liabilities  
 $= (\text{Rs. } 3,60,000 + \text{Rs. } 4,00,000) - \text{Rs. } 3,80,000 = \text{Rs. } 3,80,000$   
 Fixed assets = Rs. 3,80,000 x 80/20 = Rs. 15,20,000
- (xi) Total long term funds = Fixed Assets + Working Capital  
 $= \text{Rs. } 15,20,000 + \text{Rs. } 3,80,000 = \text{Rs. } 19,00,000$
- (xii) Capital gearing ratio being 30% (Preference share capital plus debentures to Total Long Term Funds)  
 $= 30\% \text{ of Rs. } 19,00,000 = \text{Rs. } 5,70,000$   
 Preference share capital = Rs. 5,70,000 x 2/3 = Rs. 3,80,000
- (xiii) Debentures = Rs. 5,70,000 x 1/3 = Rs. 1,90,000
- (xiv) Equity Shareholders' Fund = Rs. 19,00,000 – Rs. 5,70,000 = Rs. 13,30,000  
 General reserve and Profit & Loss Account = 20% of equity shareholders' fund  
 $= 20\% \text{ of Rs. } 13,30,000 = \text{Rs. } 2,66,000$   
 Equity share capital = Rs. 13,30,000 – Rs. 2,66,000 = Rs. 10,64,000
- (xv) Net profit = 10% of Equity share capital = Rs. 1,06,400
- (xvi) General Reserve = Rs. 2,66,000 – Rs. 1,06,400 = Rs. 1,59,600
-

## TAX LAWS

Time allowed : 3 hours

Maximum marks : 100

*NOTE : All references to sections mentioned in Part - A of the Question Paper relate to the Income-tax Act, 1961 and the relevant Assessment Year 2009-10m unless stated otherwise.*

### PART A

*(Answer Question No. 1 which is COMPULSORY and ANY THREE of the rest from this part)*

#### Question 1

- (a) *State, with reasons in brief, whether the following statements are correct or incorrect. Attempt any five :*
- (i) *Income from vacant plot of land is taxable under the head 'income from other sources'.*
  - (ii) *The maximum income of Rs.2,25,000 is not chargeable to income-tax in case of a citizen woman of 65 years age.*
  - (iii) *Due date for filing of return of income of an individual is 31st July of the previous year.*
  - (iv) *No deduction is allowable from income from salary.*
  - (v) *Indexation of cost of acquisition is necessary for short-term capital gain.*
  - (vi) *Return of income once filed cannot be revised.*
  - (vii) *Gift from an unrelated person is tax-free upto Rs. 50,000. (1 mark each)*
- (b) *Re-write the following sentences after filling-in the blank spaces with appropriate word(s)/figure(s) :*
- (i) *Income of a business commenced on 1st March, 2009 will be assessed during the assessment year \_\_\_\_\_.*
  - (ii) *Belated return can be filed within \_\_\_\_\_ from the end of the relevant assessment year.*
  - (iii) *Fringe benefit tax is charged at the rate of \_\_\_\_\_.*
  - (iv) *Advance tax is payable in \_\_\_\_\_ instalments by a non-corporate assessee.*
  - (v) *Net wealth computed under the Wealth-tax Act, 1957 shall be rounded off to the multiple of Rs. \_\_\_\_\_ . (1 mark each)*
- (c) *Robbert, a US national came to India for the first time on 1st November, 2008 for a period of six months. He declared following incomes during the previous year ending 31st March, 2009 :*
- (i) *Salary received in India for four months at the rate of Rs.75,000 per month.*
  - (ii) *Interest on fixed deposit in a bank in India : Rs.50,000.*

(iii) *Income from agriculture in USA : Rs. 10,00,000.*

(iv) *Income from a business in Nepal being controlled from India : Rs. 2,00,000.*

(v) *Salary earned in USA brought into India in the previous year : Rs. 5,00,000.*

*You are required to compute Robbert's taxable income and tax liability for the assessment year 2009-10. (5 marks)*

**Answer 1(a)(i)**

**True**

Vacant plot of land not covered under the chargeable Section 22 under the head Income from House Property. Therefore, income from Vacant Plot of land is taxable under the head "Income from other sources".

**Answer 1(a)(ii)**

**True**

For an individual whether man or woman resident in India who is of the age of 65 years or more at any time during the previous year the maximum amount not chargeable to tax is Rs. 2,25,000.

**Answer 1(a)(iii)**

**False**

Due date for filing of return of income of an individual is 31st July of the Assessment Year not previous year.

**Answer 1(a)(iv)**

**False**

Entertainment allowance and tax on employment deduction under Section 16 are allowed under the head 'Income from salaries'.

**Answer 1(a)(v)**

**False**

Indexed cost of acquisition is necessary only in case of long-term capital gain not in short-term capital gain as per explanation (iii) to Section 48.

**Answer 1(a)(vi)**

**False**

A return furnished under Section 139(1) or in pursuance of a notice under Section 142(1) can be revised under Section 139(5).

**Answer 1(a)(vii)**

**True**

Gifts from unrelated persons is taxable under the head other sources if aggregate amount exceeds Rs. 50,000.

**Answer 1(b)**

- (i) Income of a business commenced on 1st March, 2009 will be assessed during the assessment year **2009-10** .
- (ii) Belated return can be filed within **One Year** from the end of the relevant assessment year.
- (iii) Fringe benefit tax is charged at the rate of **30% plus surcharge (if any) plus education cess and SHEC @3 %**.
- (iv) Advance tax is payable in **three** instalments by a non-corporate assessee.
- (v) Net wealth computed under the Wealth-tax Act, 1957 shall be rounded off to the multiple of Rs. **100** .

**Answer 1(c)**

**Computation of Robbert's Taxable income and Tax liability  
for the Assessment Year 2009-10**

	<i>Rs.</i>
1. Income under head Salaries	
Salary 75,000 x 4	3,00,000
2. Income from other sources	
Interest on fixed deposit	50,000
Gross Total Income:	3,50,000
<i>Less</i> : Deductions u/s 80C to 80U	—
Taxable Income:	3,50,000
Tax Liability:	
Upto 1,50,000	Nil
1,50,001 to 3,00,000 @ 10%	15,000
3,00,001 and above @ 20%	10,000
	25,000
<i>Add</i> : Education Cess & SHEC @ 3%	750
Tax Liability	25,750

**Notes:**

1. Income from agriculture in USA: Not taxable in the hands of non-residents as accrue or arise outside India and received outside India.
2. Income from a business in Nepal being controlled from India: Not taxable in the hands of non-resident as Income accrues or arises and received outside India from a business controlled from India.
3. Salary received in USA brought into India in the previous year: Not taxable in the hands of non-resident as accrues or arise outside and received outside India and remitted to India in the previous year.



**Question 2**

(a) Choose the most appropriate answer from the given options in respect of following having regard to the provisions of the Income-tax Act, 1961 :

(i) The maximum penalty for failure to get accounts audited under section 44AB or furnish audit report along with return of income is —

- (a) Rs.10,000
- (b) Rs.20,000
- (c) Rs.50,000
- (d) Rs.1,00,000.

(ii) The amount of education cess and secondary and higher education cess to be collected along with income-tax for assessment year 2009-10 shall be—

- (a) 1%
- (b) 2%
- (c) 3%
- (d) 4%.

(iii) Deduction under section 80C can be claimed for fixed deposit made in any scheduled bank, if the minimum period of deposit is —

- (a) 5 years
- (b) 8 years
- (c) 10 years
- (d) 12 years.

(iv) X is the owner of a house, the details of which are given below :

Municipal value	Rs. 30,000
Actual rent	Rs. 32,000
Fair rent	Rs. 36,000
Standard rent	Rs. 40,000.

The gross annual value would be —

- (a) Rs. 36,000
- (b) Rs. 35,000
- (c) Rs. 30,000
- (d) Rs. 40,000.

(v) Interest-free loan to an employee, where the amount of loan does not exceed any one of the following, shall be treated as the tax-free perquisite in all cases under section 17(2) —

- (a) Rs. 10,000
- (b) Rs. 15,000
- (c) Rs. 20,000
- (d) Rs. 25,000.

(vi) *The maximum exemption in respect of transport allowance granted to an employee to meet his expenditure for the purpose of commuting between the place of his residence and the place of his duty shall be —*

(a) *Rs. 600 per month*

(b) *Rs. 700 per month*

(c) *Rs. 800 per month*

(d) *Rs. 900 per month.*

*(1 mark each)*

(b) *John, Jack and Jill are partners sharing profits and losses in the ratio of 2:1:1 respectively. Their summarised profit and loss account for the year ending 31st March, 2009 is appended below :*

	Rs.		Rs.
Office salaries	17,040	Gross profit	1,81,710
Bad debts reserve	3,000	Interest on	
Telephone	6,000	securities	12,000
Salary to Jack	9,000	Rent received	18,000
Collection charges of interest on securities	150		
Interest on loan from John	6,000		
Municipal taxes (let out property)	3,000		
Commission to partners :			
John	12,000		
Jack	15,000		
Jill	<u>18,000</u>		
	45,000		
Net profit to partners :			
John	61,260		
Jack	30,630		
Jill	<u>30,630</u>		
	<u>1,22,520</u>		
	<u>2,11,710</u>		<u>2,11,710</u>

*Compute total income of the firm for the assessment year 2009-10 and tax liability thereon. Interest paid to John has been calculated at the rate of 20% per annum simple. (7 marks)*

(c) *Yash, a minor, who is a physically handicapped (suffering from disability of the nature specified in section 80U), earns bank interest of Rs.50,000 and Rs.60,000 from making bags manually by himself. State whether income of Yash should be clubbed with the income of his parents as per section 64(1A). (2 marks)*

**Answer 2(a)**

- (i) Rs.1,00,000
- (ii) 3%
- (iii) 5 years
- (iv) Rs.36,000
- (v) Rs.20,000
- (vi) Rs.800 per month

**Answer 2(b)**

**Computation of total income of the firm  
for the Assessment Year 2009-10**

	<i>Rs.</i>	<i>Rs.</i>
(i) Income under head House Property:		
— Rent received	18,000	
<i>Less</i> : Municipal taxes	<u>3,000</u>	
Net Annual Value	15,000	
<i>Less</i> : Deduction under section 24		
Standard deduction @ 30% of NAV	<u>4,500</u>	10,500
(ii) Income under head "Profit and Gains:		
— From Business or Profession		
Book Profit (see working note 1)	1,55,070	
<i>Less</i> : Remuneration to working partners Subject to section 40(b) (see working note 2)	<u>54,000</u>	1,01,070
(iii) Income from other sources:		
— Interest on Securities	12,000	
<i>Less</i> : Collection charges	<u>150</u>	11,850
Gross Total Income: (i) + (ii) + (iii)		<u>1,23,420</u>
<i>Less</i> : Deductions under Chapter VIA		Nil
Total Income:		<u>1,23,420</u>

**Working Note:**

## (1) Computation of Book Profit

Net Profit as per Profit & Loss A/c	1,22,520	
<i>Less</i> : Income taxable under other head		
— Interest on Securities	12,000	
— Rent received	18,000	(30,000)

*Add :* Inadmissible Expenses:

— Salary to Jack	9,000	
— Interest on loan from John in excess of 12% (6000 x .08/.20)	2,400	
— Bad Debt Reserve	3,000	
— Collection charges	150	
— Municipal taxes	3,000	
— Commission	45,000	62,550
Book Profit		<u>1,55,070</u>

(2) Computation of Remuneration allowable to working partners subject to maximum of:

	<i>Rs.</i>
— Rs. 50,000 or 90% of Rs. 75,000 whichever is more	67,500
— 60% of Rs. 75,000	45,000
— Balance Rs.5070 @ 40%	2,028
	<u>1,14,528</u>
Actual Remuneration	
— Salary	45,000
— Commission	9,000
	<u>54,000</u>

whichever is less is allowable. Therefore Rs.54,000 is allowed as deduction

### Answer 2(c)

The clubbing provisions of Section 64(1A) are not applicable in the following cases:

- (i) Where the minor child is suffering from any disability of the nature specified in Section 80U;
- (ii) Such income which accrues or arises to the minor child on account of manual work done by him. The income of such minor child will not be clubbed in the hands of either of the parents. Consequently, the total income of Yash will be assessed in his hands.

### Question 3

(a) Distinguish between the following :

- (i) 'Scrutiny assessment' and 'best judgement assessment'.
- (ii) 'Long-term capital gain' and 'short-term capital gain'.
- (iii) 'Exempted incomes under section 10' and 'deductions under section 80'.
- (iv) 'Previous year' and 'assessment year'.
- (v) 'Assets' and 'deemed assets' under the Wealth-tax Act, 1957.

(2 marks each)

- (b) Compute the net wealth and tax liability of assessment year 2009-10 of Sona Jewels which is engaged in jewellery business. Following are the particulars of assets on 31st March, 2009 :

	Rs.
Factory building (W.D.V)	80,00,000
Bank balance	15,00,000
Unaccounted cash	5,20,000
Silver ware	56,00,000
Gold jewellery	54,00,000
Car (W.D.V)	10,00,000
Farm house within municipal limit	25,00,000
Guest house in Britain	90,00,000

The market value of car is Rs.15 lakh. The assessee has raised a loan of Rs.50 lakh from a bank by mortgaging guest house. The loan was utilised to construct factory building. (5 marks)

### Answer 3(a)(i)

#### 'Scrutiny Assessment' and 'Best Judgement Assessment'

*Scrutiny Assessment* : Scrutiny assessment is an assessment where Assessing Officer issues a notice under Section 143(2) and makes an assessment on the basis of evidence produced by assessee under Section 143(3).

*Best Judgement Assessment* : Under Section 144, the Assessing Officer, after taking into account all relevant material which he has gathered makes assessment on its own i.e. Ex-Parte is called Best Judgement Assessment

### Answer 3(a)(ii)

#### 'Long-term capital gain' and 'Short-term capital gain'

*Long-term capital gain* : The capital asset held by assessee for more than 36 months is treated as long term capital asset. The gain on its transfer is termed as long-term capital gain.

*Short-term capital gain* :

- The gain arise on transfer of short-term capital asset is called short-term capital gain.
- A capital asset held by assessee for not more than 36 months immediately preceding the date of its transfer is known as a short-term capital asset.

### Answer 3(a)(iii)

#### 'Exempted incomes under section 10' and 'deductions under section 80'

Exempted incomes are those incomes on which income tax is not chargeable. Such incomes are neither included in the total income of the assessee nor income tax is payable on them.

In computing the total income of an assessee, the deductions specified under section 80 (80C to 80U) shall be allowed from gross total income. The aggregate amount of deductions allowable under Section 80 shall not in any case exceed the gross total income of the assessee.

**Answer 3(a)(iv)**

**‘Previous year’ and ‘Assessment year’**

Previous year under section 3 is the financial year in which income is earned. It is the financial year immediately preceding the assessment year. Income tax is charged on the total income of the previous year at the rates prescribed by the relevant Finance Act for the Assessment Year.

As per Section 2(9) assessment year means the period of 12 months commencing on the first day of April every year and ending on 31st March of the next year.

**Answer 3(a)(v)**

**‘Assets’ and ‘deemed assets’ under the Wealth-tax Act, 1957**

As per Section 2(ea) of the Wealth Tax Act, 1957, Assets means following:

- (i) Guest house, residential house and commercial building;
- (ii) Motor Car
- (iii) Jewellery
- (iv) Yachts, boats and aircrafts
- (v) Urban land
- (vi) Cash in hand (for individual and HUF in excess of Rs.50,000 and for any other person any amount not recorded in the books).

According to Section 4, there are certain assets which belong to others but includible in the net wealth of an individual. They are:

- (i) Assets transferred to spouse
- (ii) Assets held by a minor child
- (iii) Assets transferred to a person or association of persons for the benefit of individual, his/her spouse.
- (iv) Assets transferred under revocable transfers
- (v) Assets transferred by an individual to son’s wife.
- (vi) Assets transferred to person or association of persons for the benefit of son’s wife.
- (vii) Converted property
- (viii) Holder of an impartible estate.

**Answer 3(b)****Computation of Net Wealth and tax liability  
for the Assessment Year 2009-10**

	<i>Rs.</i>
— Factory building (not an asset)	Nil
— Bank balance (not an asset)	Nil
— Unaccounted cash (in case of individual whether recorded in books or not Rs.50,000 shall be exempt)	4,70,000
— Silverware (Stock-in-trade therefore not an asset)	Nil
— Gold Jewellery (Stock-in-trade therefore not an asset)	Nil
— Car (car is used in the business and depreciation is admissible on it therefore its value shall be taken at W.D.V)	10,00,000
— Farm house within Municipal limit	25,00,000
— Guest house in Britain	90,00,000
	Nil
<i>Less : Debts owed</i>	Nil
Net Wealth	1,29,70,000
Wealth Tax	1,14,700

[1% on the amount in Excess of Rs. 15,00,000  
i.e.(1,29,70,000 – 15,00,000)]

**Question 4**

- (a) *Who is liable to pay advance income-tax ? On what dates the instalments of advance tax are payable and what amount is to be paid under each instalment?*  
(4 marks)
- (b) *What are the provisions regarding deduction of tax at source from the following incomes :*
- (i) *Winnings from lottery*
  - (ii) *Payment to a resident contractor*
  - (iii) *Commission and brokerage*
  - (iv) *Payment of rent.* (2 marks each)
- (c) *Discuss the items which are disallowed as deduction under section 40(b) while computing firm's income from business and profession.* (3 marks)

**Answer 4(a)****Liability for payment of Advance Tax**

Advance tax shall be payable during a financial year in every case where the tax payable by the assessee during the year is Rs.5,000 or more

**Due date and instalments****(i) In case of companies:**

<i>Due Date</i>	<i>Amount Payable</i>
On or before 15th June	Not less than 15% of Advance Tax liability
On or before 15th September	Not less than 45% of Advance Tax liability reduced by the amount already paid
On or before 15th December	Not less than 75% of Advance Tax liability reduced by the amount already paid
On or before 15th March	Not less than 100% of Advance Tax liability reduced by the amount already paid

**(ii) In case of other assessees:**

<i>Due Date</i>	<i>Amount Payable</i>
On or before 15th September	Not less than 30% of Advance Tax liability
On or before 15th December	Not less than 60% of Advance Tax liability reduced by the amount already paid
On or before 15th March	100% of Advance Tax liability reduced by the amount already paid.

**Answer 4(b)****Deduction of Tax at Source**

- (i) *Winning from lottery (Section 194B)* : The rate of tax deduction at source is 30% + Surcharge if any + Education Cess + SHEC @ 3% on the amount exceeding Rs.5000.
- (ii) *Payment to Contractor (Section 194C)* : Income tax will be deducted at source from payment made by the specified contractee to any resident contractor. The rate of TDS is as follows :
- In case of advertising contract at the rate of 1% + Surcharge if any + Education Cess @ 2% + SHEC @ 1%.
  - In any other case @2% + Surcharge if any + Education cess @ 2% + SHEC @ 1%.
  - Income of sub-contractor, the rate of TDS is 1% + Surcharge if any + Education cess & SHEC @ 3%.
- However no TDS if the amount does not exceed Rs.20,000 at one time and Rs.50,000 in a financial year.
- (iii) *Insurance Commission (Section 194D)* : If the insurance commission is payable to resident (other than company, the rate of TDS is 10% + Surcharge if any + Education cess & SHEC @ 3%.
- In the case of domestic company the rate of TDS is 20% + Surcharge if any + Education cess & SHEC @ 3%. However, no Tax shall be deducted if the insurance commission does not exceed Rs.5,000 in the financial year.



- (iv) *Payment of Rent (Section 194-I)* : An individual or HUF who is required to get his books audited under section 44AB or other person who is responsible for paying rent to a resident shall be liable to deduct TDS at the following rates :
- (a) 15% + Surcharge if any + Education cess & SHEC @ 3% if payment is made to individual or HUF.
- (b) In other cases @ 20% + Surcharge if any + Education cess & SHEC @ 3%.

However no Tax shall be deducted if the total rent payable in the financial year does not exceed Rs.1,20,000.

#### **Answer 4(c)**

#### **Amount disallowed under section 40(b)**

In computing firms income from business or profession following items are disallowed under Section 40(b) :

- (i) Salary, bonus, commission or other remuneration paid or payable to a non-working partner.
- (ii) Payment of remuneration to partners which is not authorized by the terms of partnership deed.
- (iii) Payment of interest to partners which is not authorized by partnership deed.
- (iv) Payment of remuneration authorized by partnership deed relating to any period prior to the date of partnership deed.
- (v) Payment of interest authorized by partnership deed allowed to any partner exceeding 12% per annum.
- (vi) Payment of remuneration authorized by partnership deed to any working partner exceeding the specified limit as given below:
- (1) *In case of professional firms:*
- |   |  |
|---|--|
| (a) On the first Rs.1 lac of book profit or in case of loss | Rs.50,000 or 90% of book profit whichever is more. |
| (b) On the next Rs.1 lac of book profit                     | 60% book profit.                                   |
| (c) On the balance of book profit                           | 40% of book profit.                                |
- (2) *In case of any other firms:*
- |  |  |
|--|--|
| (a) On the first Rs.75,000 of book profit or in the case of loss | Rs. 50,000 or 90% of book whichever is more. |
| (b) On the next Rs.75,000  | 60% of book profit.                          |
| (c) On the balance of book profit                                | 40% of book profit.                          |

#### **Question 5**

- (a) *Karan made a gift to Sujata during their engagement which took place on 15th May, 2008. After their marriage which was held on 15th June, 2008, they decided to live apart owing to some reasons and they obtained a legal divorce*

on 15th September, 2008. Whether transfer made on 15th May, 2008 be included for wealth-tax purposes in the hands of Karan ? (3 marks)

(b) Discuss the taxability or otherwise of the following gifts received by Madhuri, a lady, during the financial year 2008-09 :

(i) Rs.30,000 from her elder sister.

(ii) Rs.50,000 from the daughter of her elder sister.

(iii) Wrist watch valued at Rs.6,000 from her friend. (3 marks)

(c) Gaurav, aged 50 years, is an individual, whose gross total income before deduction under section 80C is Rs.1,90,000 and his total income after deduction under section 80C is Rs.95,000. Whether he is required to file return ? (3 marks)

(d) Kundan submits the following information for the assessment year 2009-10 :

Income from business	Rs. 20,000	
Property income	House-A (Rs.)	House-B (Rs.)
Municipal valuation	17,500	40,000
Municipal taxes paid by tenant	1,500	2,000
Land revenue paid	1,000	8,000
Rent received	19,000	34,000
Insurance premium paid	250	1,000
Repairs paid by tenant	250	9,000
Interest on borrowed capital for payment of municipal tax of house property	100	200
Nature of occupation	Let out for residence	Let out for business
Date of completion of construction	1.4.1993	1.4.1991

Determine the taxable income of Kundan for the assessment year 2009-10. (6 marks)

#### Answer 5(a)

The existence of husband and wife relationship is necessary not only on the date of transfer but also on the valuation date. Thus, if transfer is effected before the marriage is solemnized, or although the transfer is effected during subsistence of marriage, but on the valuation date such relationship is terminated, then in both the cases, the value of assets cannot be included in the net-wealth of the transferor.

Therefore, gift made by Karan to Sujata during their engagement shall not be included for wealth tax purposes in the hands of Karan.

#### Answer 5(b)

(i) As per section 56(2)(vi), any sum of money received from a relative shall not be treated as income. Here, Rs. 30,000 received from her elder sister. Sister is covered in the definition of relative. Hence, the gift is not taxable under the head other sources.

- (ii) As per Section 56(2)(vi), any sum of money, the aggregate value of which exceeds Rs.50,000 from unrelated persons shall be chargeable to tax. Here, the amount does not exceed Rs. 50,000, hence not taxable.
- (iii) A plain reading of Section 56(2)(vi) indicates that only sums of money received towards gift fall in its purview, gifts in kind are not liable to tax there under, hence the gift of watch is not taxable.

### Answer 5(c)

The fourth proviso to Section 139(1) requires every person, whose total income without giving effect to the provisions of Section 10A, 10B, 10BA and Chapter VIA exceeds maximum amount not chargeable to tax, to compulsorily furnish the return of income. The total income of Mr. Gaurav, before deduction under Section 80C exceeds the taxable limit of Rs. 1,50,000. Therefore, Mr. Gaurav has to compulsorily file his return of income.

### Answer 5(d)

#### Computation of Taxable Income for the Assessment Year 2009-10

(1) Income from House Property

#### House A

Gross Annual Value:

(i) Municipal Valuation	17,500
(ii) Actual rent	<u>19,000</u>
whichever is higher	19,000
<i>Less</i> : Municipal taxes	---
(Not allowed as paid by tenant)	<u>          </u>

Net Annual Value 19,000

<i>Less</i> : Standard deduction	
30% of Net Annual Value	<u>5,700</u>
	13,300

#### House B

Gross Annual Value:

(i) Municipal Valuation	40,000
(ii) Actual rent	<u>34,000</u>
whichever is higher	40,000
<i>Less</i> : Municipal taxes	---
(Not allowed as paid by tenant)	<u>          </u>

Gross Annual Value 40,000

<i>Less</i> : Standard deduction	
30% of Net Annual Value	<u>12,000</u>
	28,000

Income from House Property (13,300 + 28,000)	41,300
(2) Income from business	20,000
Gross Total Income (1) + (2)	<u>61,300</u>
Less : Deductions (Sections 80C to 80U)	—
Taxable Income	<u>61,300</u>

*Note :* Interest on borrowed capital for payment of municipal tax is not allowed as deduction under Section 24 of the Act.

### Question 6

- (a) Discuss the provisions relating to incidence of wealth-tax. (5 marks)
- (b) What are deemed fringe benefits ? (5 marks)
- (c) State, with reasons in brief, whether the following are capital or revenue receipts/ expenditure :
- Rs. 20,000 spent in connection with obtaining a licence for running a cinema hall.
  - Rs. 3,00,000 received as compensation for termination of contract of agency.
  - Lump sum received as advance rent.
  - Overhaul expenses of second hand machinery.
  - Payment to an employee to retain him in job. (1 mark each)

### Answer 6(a)

#### Incidence of Wealth Tax

Incidence of tax in the case of an individual depends upon his residential status and nationality. Residential status is decided as per the provisions of the Income-tax Act.

The scope of liability to wealth tax is as follows:

- In the case of an individual who is a citizen of India and resident in India, a resident HUF and company resident in India;
 

Wealth tax is chargeable on net wealth comprising of:

  - All assets in India and outside India;
  - All debts in India and outside India are deductible in computing the net wealth.
- In the case of an individual who is a citizen of India but non-resident in India or not ordinarily resident in India, HUF, non-resident or not ordinarily resident in India and a company non-resident in India;
  - All assets in India are chargeable to tax.
  - All debts in India are deductible in computing the net wealth.
  - All assets and debts outside India are out of the scope of Wealth Tax Act.

- (iii) In the case of an individual who is not a citizen of India whether resident, non-resident or not ordinarily resident in India:
  - (a) All assets in India are chargeable to tax.
  - (b) All debts in India are deductible in computing the net wealth.
  - (c) All assets and debts outside India are out of the scope of Wealth Tax Act.

### **Answer 6(b)**

#### **Deemed Fringe Benefits**

Following benefits shall be deemed to have been provided by the employer to his employees if the employer has in the course of his business and profession incurred these expenses (Section 115WB(2)).

- (i) *Entertainment* : 20% of expenditure will be considered as value of 'fringe benefit'. It includes the reimbursement of entertainment expenditure by an employer to employees/directors/others.
- (ii) *Provision of hospitality* : 20% of expenditure will be considered as value of 'fringe benefit'. It covers provision of hospitality of every kind by the employer to any person whether by way of provision of goods or beverages or in any other manner.
- (iii) *Conferences* : 20% of expenditure will be considered as value of 'fringe benefit'. It covers any expenditure on conveyance, tour and travel, on hotel, or boarding and lodging in connection with any conference.
- (iv) *Sale Promotion* : 20% of expenditure will be considered as value of 'fringe benefit'. It covers sales promotion including publicity.
- (v) *Employees Welfare* : 20% of expenditure will be considered as value of 'fringe benefit'.
- (vi) *Conveyance* : 20% is treated as fringe benefit. It includes Reimbursement of car expenses, Travelling expenditure/conveyance expenditure/tour or allowances for meeting lodging and boarding given to employees.
- (vii) *Hotel and lodging* : 20% of expenditure will be considered as value of 'fringe benefit'. It covers use of hotel, boarding and lodging facilities.
- (viii) *Repairs and maintenance of motor cars* : 20% of expenditure will be considered as value of 'fringe benefit'. It covers repair, running (including fuel) maintenance of motor cars and the amount of depreciation thereon.
- (ix) *Repairs and maintenance of aircrafts* : It covers repair, running (including fuel) maintenance of aircrafts and the amount of depreciation thereon. 20% of the expenditure will be considered as 'fringe benefit'.
- (x) *Telephones* : It covers use of telephone (including mobile phone) other than expenditure on leased telephone lines. 20% of expenditure will be considered as value of 'fringe benefit'.
- (xi) *Festival celebrations* : It includes any festival celebration expenditure but does not include expenditure on celebration of Independence Day and Republic Day.

20% of expenditure will be considered as fringe benefit from the assessment year 2009-10.

- (xii) *Use of health club and similar facilities* : It includes reimbursement of health club expenditure to employees/directors and payment of entrance fees. 50% of expenditure will be considered as value of fringe benefit.
- (xiii) *Use of any other club facilities* : It includes payment of entrance fees to club expenditure to employees. 50% of expenditure will be considered as value of fringe benefit.
- (xiv) *Gifts* : Gift may be in cash or kind. Even gifts on promotion of company's products to distributors/retailers are covered under fringe benefit. 50% of expenditure will be considered as value of fringe benefit.
- (xv) *Scholarships* : It includes expenditure on training of employees in an educational institute. 50% of expenditure will be considered as value of fringe benefit.
- (xvi) *Tour, travel, foreign travel* : 5% of expenditure will be considered as value of fringe benefit.

### Answer 6(c)

#### Capital or Revenue

- (i) The amount spent in connection with obtaining a license for running a cinema hall is a capital expenditure because it is to acquire a source of income.
- (ii) It is a capital receipt because it is in connection with a service of income.
- (iii) It is a revenue receipt because it is a lump sum payment of income.
- (iv) It is revenue expenditure because the expenditure will not increase the capacity of the machinery.
- (v) It is revenue expenditure because it is a lump sum reward to an employee from employer.

### PART B

#### Question 7

Attempt any four of the following :

- (i) *Briefly state the provisions of service tax regarding following :*
  - (a) *Liability to registration*
  - (b) *Procedure for registration*
  - (c) *Issue of registration certificate*
  - (d) *Time limit for registration*
  - (e) *Surrender of certificate of registration.* (1 mark each)
- (ii) *What is general rule regarding valuation of taxable service ? Indicate the position where the gross amount charged by a service provider includes service tax payable.* (5 marks)

- (iii) *What is the due date for payment of service tax ? What is the rate of interest for delayed payment and penalty for default in payment of service tax ? (5 marks)*
- (iv) *Discuss 'advance ruling in service tax'. (5 marks)*
- (v) *Explain the provisions regarding service tax on Company Secretaries. (5 marks)*

**Answer 7(i)**

**(a) Liability to Registration under Service Tax**

Person specified to make an application:

- (a) An input service provider
- (b) Any provider of taxable service whose aggregate value of taxable service exceed Rs. 9 lakhs.
- (b) Procedure for registration :** For registration of Service Tax every person liable for paying the service tax shall make an application to the Superintendent of Central Excise in Form ST-1 for registration within a period of thirty days from the date on which the service tax is levied under section 66.
- (c) Issue of Registration Certificate :** The registration shall be granted by the Superintendent of Central Excise within 7 days from the date of receipt of registration in FORM ST-2. If the registration certificate is not granted within the said period, the registration applied for shall be deemed to have been granted.
- (d) Time limit for registration :** Every person liable to pay service tax should make an application to the Superintendent of Central Excise within 30 days from the date service Tax levied under section 66.
- (e) Surrender of Certificate of Registration :** In the following cases the certificate of registration shall be surrendered by the assessee:
- (i) When a registered assessee transfers his business, he should surrender his registration.
- (ii) When a registered assessee ceases to carry on the service activity for which he is registered.

**Answer 7(ii)**

Under Section 67, service tax shall be chargeable on any taxable service with reference to its value. Such value will be as follows:

- (i) Where the consideration received for provisions of service is wholly in money, the value shall be the gross amount charged by the service provider for provision of service.
- (ii) Where the consideration received for provision of service is not wholly consisting of money, the value in such case shall be the gross amount charged by the service provider for provision of similar service to any other person in ordinary course of business.

- (iii) Where the provision of service is for a consideration which is not ascertainable, the value shall be determined in the prescribed manner. Where the gross amount charged by the service provider is inclusive of service tax payable, the value of such taxable service shall be such amount, as with the addition of tax payable is equal to the gross amount charged. The gross amount charged for the taxable service shall include any amount received towards the taxable service before, during or after provision of such service.

### **Answer 7(iii)**

#### **Payment of Service Tax and Due date**

Section 68 provides that every person providing taxable services to any person should pay service tax at the rate specified in Section 66. Rule 6 lays down the following rules for payment of service tax:

- (a) *In case of an individual and partnership firm* : The service tax received during any quarter shall be paid to the Government by the 5th of the month immediately following the relevant quarter.
- (b) *In case of others* : The service tax received during any calendar month should be paid to the credit of the Central Government by the 5th of the month immediately following the relevant calendar month.

#### **Interest on delayed payment of Service Tax**

Any person who has failed to pay the tax to the Government within the prescribed time limit, such person shall pay simple interest @ 13% p.a. for the period of delay.

#### **Penalty for failure to pay Service Tax**

If any person who is liable to pay service tax has failed to pay within prescribed time limit, he will be liable to pay interest @ 13% p.a. and also penalty. Penalty for failure to pay service tax shall be Rs.200 per day or 2% of such tax per month whichever is higher, starting from the first day after the due date till the date of actual payment of the outstanding amount of service tax. However, total amount of penalty shall not exceed the amount of service tax.

### **Answer 7(iv)**

#### **Advance Ruling**

Section 96A(a) defines 'Advance Ruling' as the determination, by the authority of a question of law or fact specified in the application, regarding the liability to pay service tax in relation to a service proposed to be provided by the applicant.

As per Section 96C(2), an advance ruling may be sought on a question of law or fact, in respect of –

- (a) Classification of any service as a taxable service, under Chapter V of the Finance Act, 1994.
- (b) The valuation of a taxable service for charging service tax.
- (c) The principles to be adopted for the purposes of determination of value of the taxable services.



- (d) Applicability of notifications issued under Chapter V of the Finance Act, 1994.
- (e) Admissibility of credit of service tax.
- (f) Determination of the liability to pay service tax on a taxable service under the provisions of Chapter V.

**Questions not to be considered for Advance Ruling**

An application for Advance Ruling on a question shall not be entertained if:

- (a) The same question is already pending in a case before any Central Excise Authority, Appellate Tribunal or any Court, or
- (b) It is the same as in a matter already decided by the Appellate Tribunal or Court.

**Persons Eligible to seek Advance Ruling**

As per Section 96A(b) an application for Advance Ruling may be made by following persons:

- (a) A non-resident setting up a joint venture in Indian in collaboration with a non-resident or a resident and proposing to undertake a business activity in India.
- (b) A resident setting up a joint venture in India in collaboration with a non-resident, and proposing to undertake business activity in India;
- (c) A wholly owned subsidiary Indian company of a foreign holding company, proposing to undertake a business activity in India.
- (d) A joint venture in India;
- (e) A resident falling within a notified class or category of persons.

**Application for obtaining Advance Ruling**

A person desiring to obtain an Advance Ruling shall make an application in Form AAR-ST (quadruplicate).

**Answer 7(v)**

“Practising Company Secretary” is a person who is a member of the Institute of Company Secretaries of India and is holding a certificate of practice granted under the provisions of the Company Secretaries Act, 1980 and includes any concern engaged in rendering services in the field of Company Secretary Ship.

Taxable service means any service provided to a client, by a practicing company secretary in his professional capacity, in any manner.

The following are the taxable services in case service provided by the company secretaries are:

- (i) Accounting and auditing; or
- (ii) Cost accounting and cost auditing; or
- (iii) Secretarial auditing; or

- (iv) Certification under Companies Act.
- (v) Certification for exchange control purposes under FEMA.

**Value of Taxable Service:**

In the case of Practising Company Secretary—“Value of taxable service shall be the gross amount charged by the service provider for such services rendered by him.

Service tax is charged only on the Practising Company Secretary not on company secretary who are in services (employment).

**PART C**

**Question 8**

*Answer any two of the following :*

- (i) *Who is liable to pay VAT ? Discuss the advantages of introduction of VAT in India. (10 marks)*
- (ii) *Discuss — (a) Rates of VAT; and (b) Filing of return under VAT. (10 marks)*
- (iii) *Discuss, with suitable example, various methods for computation of VAT liability. (10 marks)*
- (iv) *Write notes on — (a) Registration under VAT; and (b) Zero rating. (10 marks)*

**Answer 8(i)**

**Liability to pay VAT**

With the objective of tax reform at the state level, the Vat was introduced in India on the recommendation of the Empowered Committee of State Finance Minister headed by the Bengal Finance Minister Dr. Asim Dasgupta. The white paper submitted by the committee specified that only those dealer whose annual gross turnover was more than Rs.5 lacs required registration under Vat Act. However, the Committee has subsequently allowed the states to increase the limit from Rs.5 lacs to 10 lacs. It was also suggested that the concerned state shall have to bear the revenue loss on account of increase in the limit beyond Rs.5 lacs.

**Advantages**

1. *No tax evasion* : The system is logical and scientific. Credit of duty/tax is allowed against the liability on the final product manufactured or sold. For this purpose, proper records have to be maintained. In that case tax evasion would become difficult.
2. *Neutrality* : The system does not interfere in the choice of decision to make purchases. As the effect of the system is anti-cascading, the amount of addition to value or the stage at which it is made is not of any relevance.
3. *Certainty* : VAT is a simple procedure relying not transactions only without definitions of sale, sale price etc. and therefore results in certainty of revenue collection.
4. *Transparency* : The buyers will have full transparency of tax component. Government will be enabled to take proper decisions in respect of tax rates.

5. *Better revenue collection* : In Vat, possibility of leakage of revenue is minimum because tax credit can be availed only on proof of payment of tax at an earlier stage is produced. Even if tax is evaded at one stage, it will invariably be collected at the subsequent or final stage or from a person who is not able to produce such a proof. Thus, an invoice of VAT will be self-enforcing which naturally results in a stable source of revenue to Government.
6. *Better accounting systems* : The system of availing VAT credit of earlier stages will bring about a compliance of proper maintenance of accounts.
7. *Effect on retail price* : The system of availing credit of tax paid at earlier stages will not only remove cascading effect of taxation but also curb the inflationary trend in prices of goods.

### **Answer 8(ii)**

#### **Rates of VAT**

To reduce the multiplicity of sales tax rates between various states in India it was recommended that Vat will have broadly four tax rates:

- (a) Zero rate or tax free goods;
- (b) 1% on precious and semi precious metals i.e. bullion etc.
- (c) 4% on declared goods;
- (d) 20% on luxury goods;
- (e) 12.5% on other goods.

#### **Filing of return under VAT**

Returns are to be filed monthly/quarterly/annually along with tax paid challans according to the provisions of State Act. They should contain details of output tax liability, value of input tax credit and payment of VAT and filed within the prescribed time schedule. In case of any mistakes, revised returns may be filed. The returns will be checked and any deficiency in payment of tax may have to be made good.

*Filing of returns are designed with a view*

- (i) To reduce cost of compliance
- (ii) To encourage business to comply with their obligations; and
- (iii) To ensure efficient processing of data.

### **Answer 8(iii)**

#### **Methods for computation of VAT**

##### ***Invoice Method***

Under this method tax is imposed at each stage of sale on the total sale value and the tax paid on inputs is set-off. Indian states have opted for invoice method which is similar to CENVAT. The possibility of tax evasion can be minimized under this system.

VAT payable = Total tax charged on the outputs or sales

Less : Total tax paid to the on inputs sales or purchases

*Example:*

Suppose 'A' is dealer in the State who has made purchases of goods taxable @ 12.5% of Rs. 75/- from outside the State. He sells these goods at Rs.100/- to another dealer 'B' in the State. The dealer 'B' further makes the sale of the goods at Rs. 150/- to another dealer 'C' in the State who in turn sells the goods to the consumer at Rs. 200/. The Sales prices are exclusive of Vat. The VAT payable by each of the dealers A, B & C is as follows:

<i>Dealer</i>	<i>Tax on Sale – Tax on Purchase</i>	<i>Tax Payable</i>
A =	12.5 - 0	12.5
B =	18.75 -12.5	6.25
C =	25 – 18.75	6.25

Total Tax Payable: 12.5+6.25+6.25 =25 or 12.5% of Rs.200 i.e. Rs.25

#### ***Subtraction Method***

This is a cost subtraction credit which is also a simple method. Under this method tax is collected only on value addition at each stage of sale and hence the question of giving set off of tax accredit does not arise. This method is applied in cases where tax is not separately charged.

Take the same example as above:

Here the tax is calculated on the value addition therefore the question of set off can not arise. The Sale price is inclusive of Tax.

<i>Dealer</i>	<i>Value addition</i>	<i>Tax Payable</i>
A	112.5	$(110 \times 12.5) / 100 + 12.5$ = 10
B	168.75 -112.5=56.25	$(56.25 \times 12.5) / 100 + 12.5$ = 6.25
C	225 – 168.75=56.25	$(56.25 \times 12.5) / 100 + 12.5$ = 6.25

**Total Tax Payable : Rs.25/-**

#### ***Additional Method***

Calculate all the value additions i.e., labour expenses and profit, if the labour Rs.100 and expenses are Rs.500. Add all the expenses and profit say Rs.100+ 500+ 400 (Profit)= 1000 and calculate 12.5% of Rs.1000 and this amount is Rs.125 and this is the tax payable by the dealer. Since the tax is payable on addition of all expenses and profit hence this is called addition method of calculation of tax.

**Answer 8(iv)****(a) Registration under VAT**

All dealers are required to get registration under the Vat law. Only then, he as a registered dealer can carry on his business of purchasing and selling goods on payment of VAT.

*Requirement for registration* : All dealers with gross turnover exceeding Rs.5 lakhs will get the registration. All existing dealers will automatically get registered under the Vat Act. New dealers will be allowed 30 days time from the date of tax liability to get registered. An application is to be made to the Commissioner for this purpose.

*Compulsory registration* : In case an assessee fails to get registration, he will be compulsorily registered by the Commissioner, after assessing his tax liability on the basis of evidence available with him. Failure to get registered will attract penalty for default and forfeiture of eligibility to avail input tax credit and set off of tax.

*Voluntary registration* : A dealer who does not require registration can voluntarily obtain it after satisfaction of the Commissioner regarding the requirement.

*Cancellation of registration* : A registration can be cancelled on:

- (i) discontinuance of business; or
- (ii) disposal of business; or
- (iii) transfer of business to a new location; or
- (iv) annual turnover falling below the specified limit.

**(b) Zero Rating**

Zero rating means that the tax payable on sale of a commodity is fixed at 0%. Though apparently, it looks similar to an exempt transaction, there is a significant difference between the two. While in an exempt transaction, the tax paid on input lapses i.e., it cannot be set off, under the Zero rated sales, prior stage tax is set off against the 0% tax paid, and effectively the entire tax paid on purchases is eligible for refund. Thus, Zero Rating is advantageous to the dealer compared to exempting of sale transactions. Generally, export sales are zero rated and thereby, exporters are granted refund of taxes paid by them on their inputs. Exporters gain significantly due to the Zero Rating.

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## EXECUTIVE PROGRAMME

JUNE 2009

### COMPANY LAW

*Time allowed : 3 hours*

*Maximum marks : 100*

**NOTE :** 1. Answer **SIX** questions including Question No. 1 which is **COMPULSORY**.

2. All references to sections relate to the Companies Act, 1956 unless stated otherwise.

#### **Question 1**

*Comment on any four of the following :*

- (i) *An unlimited company is a company not having any limit on the liability of its members.*
- (ii) *A company can mortgage or charge any part of its 'reserve capital'.*
- (iii) *There is no statutory requirement that a director must hold qualification shares in the company in which he is a director.*
- (iv) *Statutory meeting can be held at any time and place as suited to the company.*
- (v) *Provisions of section 58A are not applicable to guarantee companies and section 25 companies (i.e., associations not for profit). (5 marks each)*

#### **Answer 1(i)**

*The statement is correct.* As per Section 12(2)(c) of the Companies Act, 1956, an "unlimited company" is a company not having any limit on the liability of its members. Thus, the maximum liability of the member of such a company, in the event of its being wound up, might stretch up to the full extent of their assets to meet the obligations of the company by contributing to its assets. However, the members of an unlimited company are not liable directly to the creditors of the company, as in the case of partners of a firm. The liability of the members is only towards the company and in the event of its being wound up only the liquidator can ask the members to contribute to the assets of the company which will be used in the discharge of the debts of the company.

An unlimited company may or may not have share capital. The articles of association of an unlimited company must state the number of members with which the company is to be registered and if the company has share capital, the amount of share capital with which the company is to be registered [Section 27(1)].

#### **Answer 1(ii)**

*The statement is not correct.* A company may charge its uncalled capital if its articles or memorandum may give an express power to charge uncalled capital, or the power may be so wide that it can be inferred by implication. For example, in *Newton v. Debentureholders of Anglo Australian Investment Co.* (1895) AC 224, the memorandum authorized the company to borrow "upon any security of the company" it was held that the power was wide enough to include a charge on uncalled capital.

However, a company cannot mortgage or charge any part of its “reserve capital”. Reserve capital is that part of the uncalled capital of a company which the limited company has decided by special resolution in terms of Section 99 of the Companies Act, 1956, not to call except in the event and for the purpose of the company being wound up. (Section 98 and 99 of the Companies Act, 1956).

**Answer 1(iii)**

*The statement is correct.* There is no statutory requirement that a director must hold qualification shares in the company in which he is a director. Thus, a person may be a director in a company without being its member unless the articles provide otherwise. However, the articles usually provide for a share qualification. The modern view is that holding a nominal share qualification does not make a director more responsible. If the articles of a company provide for share qualification, section 270 lays down that –

- (a) Each director must obtain his qualification shares within two months after his appointment as a director.
- (b) Any provision in the articles shall be void in so far as it requires a person to hold the qualification shares before his appointment as a director or to obtain them within a shorter time than 2 months after his appointment as such.
- (c) The nominal value of the qualification shares shall not exceed Rs.5,000 or the nominal value of one share where it exceeds Rs. 5,000.
- (d) For the purpose of any provision in the articles requiring a director to hold a specified share qualification, the bearer of a share warrant should not be deemed to be the holder of the shares specified in the warrant. It was also held in the case of *Spencer v. Kennedy* (1926) ch 125 that a person cannot be said to be qualified in respect of qualification shares until he is registered as holder of the shares.

**Answer 1(iv)**

*The statement is correct.* According to Section 165(1) of the Companies Act, 1956: “Every company limited by shares, and every company limited by guarantee and having a share capital, shall, within a period of not less than one month and not more than six months from the date at which the company is entitled to commence business, hold a general meeting of the members of the company, which shall be called “the statutory meeting.”

Section 165(10) provides that the provisions of Section 165 are not applicable to a private company. It therefore follows that statutory meetings are required to be convened only by a public company limited by shares or limited by guarantee and having a share capital. Thus such meetings are not required to be held by a company limited by guarantee and not having a share capital or by a private company.

So, section 165 of the Companies Act, 1956 does not specify time and place for holding a statutory meeting. Hence, it can be assumed that a statutory meeting can be held at any time and place as suited to the company.

**Answer 1(v)**

*The statement is not correct.* The provisions of section 58A and 58B of the Companies Act and Companies (Acceptance of Deposits) Rules are also applicable to

companies limited by guarantee and associations not for profit viz., section 25 companies, having share capital and formed for promoting commerce, art, science, religion, charity etc. However, guarantee companies which have no share capital have to comply with the requirements of the provisions of these sections and rules to the extent applicable.

### Question 2

(a) *Re-write the following sentences after filling-in the blank spaces with appropriate word(s)/figure(s) :*

- (i) *Without the consent of the general meeting, the Board of directors can borrow money subject to a maximum of \_\_\_\_\_.*
- (ii) *A \_\_\_\_\_ though entitled to attend a general meeting and vote on a poll, but cannot participate in the discussion.*
- (iii) *Besides making investment and loans, a company can also provide \_\_\_\_\_ and security to another company.*
- (iv) *A sole buying agent who holds a substantial interest in excess of 5% of the paid up share capital of the company or Rs. \_\_\_\_\_ whichever is the lesser, can be appointed only with the prior approval of the Central Government.*
- (v) *A promoter can earn profit out of sale of his own property to the company by making \_\_\_\_\_, otherwise he has to account for the profits to the company.*
- (vi) *An issue of debentures by a listed public company needs to maintain post-issue debt equity ratio of 2:1 as per \_\_\_\_\_.*
- (vii) *Allotment of shares in a public issue without receiving minimum subscription amounts to \_\_\_\_\_.*
- (viii) *A member cannot ask for inspection of minutes of \_\_\_\_\_.*

(1 mark each)

(b) *Choose the most appropriate answer from the given options in respect of the following :*

- (i) *A company is —*
  - (a) *A voluntary association for profit*
  - (b) *A compulsory association for profit*
  - (c) *A statutory association for profit*
  - (d) *None of the above.*
- (ii) *A private company need not hold —*
  - (a) *Extra-ordinary general meeting*
  - (b) *Statutory meeting*
  - (c) *Annual general meeting*
  - (d) *Board meeting.*
- (iii) *As per section 252(2), a private company cannot have less than —*
  - (a) *3 Directors*



- (b) 2 Directors
  - (c) 5 Directors
  - (d) 7 Directors.
- (iv) Who cannot become a member of a company —
  - (a) Company as a member of another company
  - (b) Foreigner
  - (c) Trade union
  - (d) Partnership firm.
- (v) Section 125 requires a company to file prescribed particulars of charge after the date of creation of a charge with the Registrar of Companies within—
  - (a) 30 Days
  - (b) 60 Days
  - (c) 90 Days
  - (d) None of the above.
- (vi) Change of registered office of a company from one city to another city in the same State but falling under the jurisdiction of two Registrars of Companies is required to be approved by the —
  - (a) Central Government
  - (b) Registrar of Companies
  - (c) Regional director
  - (d) Company Law Board.
- (vii) A public company can be converted into a private company only after the approval of the —
  - (a) High Court
  - (b) State Government
  - (c) Central Government
  - (d) Company Law Board.
- (viii) As per the Companies Act, 1956, the types of resolutions to be passed by the shareholders are —
  - (a) 5
  - (b) 4
  - (c) 2
  - (d) 3.

(1 mark each)

**Answer 2(a)**

- (i) Without the consent of the general meeting, the Board of directors can borrow money subject to a maximum of **the aggregate of Company's paid-up capital and free reserves** .

- (ii) A **proxy** though entitled to attend a general meeting and vote on a poll, but cannot participate in the discussion.
- (iii) Besides making investment and loans, a company can also provide **guarantee** and security to another company.
- (iv) A sole buying agent who holds a substantial beneficial interest in excess of 5% of the paid up share capital of the company or Rs. **5,00,000** whichever is the lesser, can be appointed only with the prior approval of the Central Government.
- (v) A promoter can earn profit out of sale of his own property to the company by making **disclosure** , otherwise he has to account for the profits to the company.
- (vi) An issue of debentures by a listed public company needs to maintain post-issue debt equity ratio of 2:1 as per **SEBI Guidelines** .
- (vii) Allotment of shares in a public issue without receiving minimum subscription amounts to **irregular allotment** .
- (viii) A member cannot ask for inspection of minutes of **Meetings of Board of Directors**.

**Answer 2(b)(i)**

- (a) A voluntary association for profit

**Answer 2(b)(ii)**

- (b) Statutory meeting

**Answer 2(b)(iii)**

- (b) 2 Directors

**Answer 2(b)(iv)**

- (d) Partnership firm

**Answer 2(b)(v)**

- (a) 30 days

**Answer 2(b)(vi)**

- (c) Regional director

**Answer 2(b)(vii)**

- (c) Central Government

**Answer 2(b)(viii)**

- (d) 3

**Question 3**

- (a) *In what manner 'membership' in a company can be sought ?* (8 marks)
- (b) *What are the modes in which a director of a company can be appointed ?* (8 marks)

**Answer 3(a)****Seeking of membership in a company**

As per section 41 of the Companies Act, 1956, in the following manner, a membership in a company is obtained:

- (i) By subscribing to the Memorandum of Association of a company at the time of incorporation of the company.
- (ii) By transfer – a person can get shares transferred in his name and cause his name to be entered in the register of members maintained by the company.
- (iii) By transmission – on a death of a member or insolvency his shares could be inherited by succession or will.
- (iv) By an application in writing – under an invitation in public issue or otherwise, a person can make application for allotment of shares (by making an offer to the company) and company accepting in the form of allotment.
- (v) Allotment by estoppel – If a person allows his name to be entered in the Register of Members of a company, then he is estopped from denying his membership.
- (vi) As a beneficial owner – under dematerialized form every person holding equity share capital of company and whose name appears in the record of depository, he shall be deemed to be member.

**Answer 3(b)****Appointment of directors**

Following are the ways by which a person can be appointed as a director:

- (i) *By subscription to the memorandum* – at the time of incorporation the person who subscribes to the memorandum becomes automatically a director unless Articles of Association mention names of First Directors. He shall hold office until the conclusion of the First Annual General Meeting (Section 254 of the Companies Act, 1956).
- (ii) *By members at General Meeting* – It is the prerogative of the members to appoint a person as a director at a general meeting. Provisions in this regard are contained in section 255, 256, 257 and 265 of the Companies Act, 1956.
- (iii) *By Board of Director* – the Board of Directors can appoint Directors in certain circumstances –
  - As an additional director under section 260 – such additional director shall hold office only upto date of the next annual general meeting of the company.
  - To fill up casual vacancy under section 262 – such person shall hold office only upto the date upto which the director in whose place he is appointed would have held the office if it had not been vacated the office.
  - As an alternate director under section 313 – An alternate director shall not hold office as such for a period longer than that permissible to the original

director in whose place he has been appointed and shall vacate office if and when the original director returns to the state in which Board meetings are ordinarily held.

- (iv) *By Third Party duly authorized* – a nominee director can be appointed by third parties like banks, financial institution or other lenders etc. They can nominate a director to represent their interest on the Board.
- (v) *By Central Government* – Section 408 of the Act, vests overriding powers in Central Government to nominate directors. Sub-section (1) of this section provides that the Central Government may appoint such number of persons as directors as the Company Law Board may, by order in writing specify. Moreover, the appointment shall be made, if the Company Law Board, on a reference made to it by the Central Government or on an application of not less than one hundred members of the company or of the members of the company holding not less than one-tenth of the total voting power therein, is satisfied after such inquiry that it is necessary to make such an appointment of directors.
- (vi) *By small shareholders* – The Companies (Amendment) Act, 2000 has empowered small share holders in a company to send their representative as a director on the Board. The small holder means a shareholder holding shares of nominal value of twenty thousand rupees or less in a public company. The preconditions for such representative as provided in section 252(1) of the Companies Act, 1956 are –
  - (a) The paid-up capital of the company must be Rs.5 crore or more and
  - (b) No. of small shareholders is 1000 or above.

#### Question 4

*Write short notes on any four of the following :*

- (i) *Doctrine of ultra vires.*
- (ii) *Doctrine of constructive notice*
- (iii) *Red-herring prospectus*
- (iv) *Managerial remuneration*
- (v) *Interim dividend.*

*(4 marks each)*

#### Answer 4(i)

##### **Doctrine of ultra vires**

“Ultra Vires” means beyond the powers of. The word ‘ultra’ means beyond and the word ‘vires’ means the powers. In the case of a company whatever is not stated in the memorandum as the objects or powers, is prohibited by the doctrine of ultra vires. As a result, an act which is ultra vires is void, and does not bind the company. Neither the company nor the other contracting party can sue on it. Also, the company cannot make it valid, even if every member assents to it.

The general rule is that an act which is ultra vires the company is incapable of ratification. An act which is intra vires the company but outside the authority of the

directors may be ratified by the company in proper form [*Rajendra Nath Dutta v. Shilendra Nath Mukherjee*, (1982) 52 Comp. Cas. 293 (Cal.)].

The rule is meant to protect shareholders and the creditors of the company. But if the act is ultra vires (beyond the powers of) the directors only, the shareholders can ratify it. Or, if it is ultra vires the articles of association, the company can alter its articles in the proper way.

#### **Answer 4(ii)**

##### **Doctrine of constructive notice**

When a company is incorporated, its Memorandum and Articles of Association are filed with the Registrar of Companies. These documents are known as public documents. Any person who wants to deal with the company is expected to know about the same. The doctrine of constructive notice implies that any person dealing with the company has not only gone through the Memorandum and Articles of Association but also has understood them. [*Griffith v. Paget* (1877) Ch.D 517]. Thus, this doctrine operates in favour of a company. It is a responsibility cast upon the public to have knowledge about these documents and it can not be a defence available to outsiders that he had no knowledge about the same. For example, if the articles provide that a bill of exchange to be effective must be signed by two directors, a person dealing with the company must see that it is so signed; otherwise he cannot claim under it.

Outsiders dealing with incorporated bodies are bound to take notice of limits imposed on the corporation by the memorandum or other documents of constitution. Nevertheless they are entitled to assume that the directors or other persons exercising authority on behalf of the company are doing so in accordance with the internal regulations as set out in the Memorandum & Articles of Association.

#### **Answer 4(iii)**

##### **Red-herring prospectus**

As per the explanation to sub-section (4) of section 60B of the Companies Act, 1956, "Red-herring prospectus" means a prospectus which does not have complete particulars on the price of the securities offered and the quantum of securities offered. The red-herring prospectus carries same obligations as are applicable in the case of prospectus. Every variation between the information memorandum and the red-herring prospectus shall be highlighted by the issuer company and shall be individually intimated to the persons invited to subscribe to the securities.

Section 60B(7) provides that the applicant or proposed subscriber shall exercise his right to withdraw from the application on any intimation of variation within seven days from the date of such intimation and shall indicate such withdrawal in writing to the company and the underwriters.

The company or underwriters or bankers shall not encash subscription moneys or post-dated cheques or stock-invest received in advance, before the date of opening of the issue, without having individually intimated the prospective subscribers of the variation and without having offered an opportunity to such prospective subscribers to withdraw their application and cancel their post-dated cheques or stock-invest or return of the subscription paid.

Once the offer of securities is closed, a final prospectus indicating quantum and price of securities offered shall be filed with ROC and SEBI.

#### **Answer 4(iv)**

##### **Managerial remuneration**

To remunerate means to pay, re-compensate, or reward for work, etc. The term managerial remuneration has not been defined in the Companies Act, 1956 (Act). The remuneration paid to directors is subject to the provisions of Section 198, 309 and Schedule XIII of the Companies Act, 1956.

Managerial remuneration may take the form of monthly payments, say, salary or a specified percentage of net profits or a commission and/or by way of a fee for each meeting of the Board (called sitting fee) Besides, as per Explanation to Section 198(4) of the Act, the expression 'remuneration' shall also include:

- (a) any expenditure incurred by the company in providing any rent free accommodation, or any other benefit or amenity in respect of accommodation free of charge, to any of its directors or manager;
- (b) any expenditure incurred by the company in providing any other benefit or amenity free of charge or at a concessional rate to any of the persons aforesaid;
- (c) any expenditure incurred by the company in respect of any obligation or service, which, but for such expenditure by the company, would have been incurred by any of the persons aforesaid; and
- (d) any expenditure incurred by the company to effect any insurance on the life of, or to provide any pension, annuity or gratuity for any of the persons aforesaid or his spouse or child.

Section 198(1) lays down 11% of the net profits as the overall ceiling on the total managerial remuneration payable by a public company or a private company, which is a subsidiary of a public company, to its directors (which means all directors including managing and whole-time directors) and manager.

#### **Answer 4 (v)**

##### **Interim dividend**

A part of profits may be distributed before the annual accounts are finally prepared, audited and passed. Such dividends are called interim dividend. The interim dividend is thus a dividend paid between two annual general meetings of the company. Sub-section (1A) of section 205 of the Companies Act, 1956 empowers the Board of Directors of a company to declare interim dividend. Regulation 86 of Table A of Schedule I to the Companies Act provides:

“The Board may from time to time pay to the members such interim dividend as appear to it to be justified by the profits of the company.”

Till the passing of the Companies (Amendment) Act, 2000, there was no provision in the Companies Act (except Reg. 86 of Table A) relating to interim dividend. The Companies (Amendment) Act, 2000 has introduced sub-section (14A) in section 2 whereby

'interim dividend' is now part of 'dividend' and accordingly all provisions of the Companies Act relating to 'dividends' have become applicable to 'interim dividend' also.

### Question 5

- (a) *What is 'floating charge' ? When does it crystallise ? What is effect of crystallisation of a floating charge ?* (8 marks)
- (b) *What are the salient features of limited liability partnership (LLP) ?* (8 marks)

#### Answer 5(a)

A floating charge as a type of security is peculiar to companies as borrowers. A floating charge is not attached to any definite property but covers property of a changing nature e.g. stock-in-trade and is thus necessarily equitable. A floating charge is a charge on a class of assets present and future which in the ordinary course of business is changing from time to time leaves the company free to deal with the property as it sees fit until the holders of charge take steps to enforce their security.

*Crystallization of floating charge :* A floating charge attaches to the company's property generally and remains dormant till it crystallizes or becomes fixed. The company has a right to carry on its business with the help of assets having a floating charge till the happening of some event which determines this right. A floating charge crystallizes and the security becomes fixed in the following cases:

- (a) When the company goes into liquidation.
- (b) When the company ceases to carry on the business.
- (c) When the creditors or the debenture holders take steps to enforce their security e.g. by appointing receiver to take possession of the property charged.
- (d) On the happening of the events specified in the deed of charge.

*Effect of crystallization of a floating charge :* On crystallization, the floating charge converts itself into a fixed charge on the property of the company. It has priority over any subsequent equitable charge or other unsecured creditors. But preferential creditors who have priority for payment over secured creditors in the winding up gets priority over the claims of the bankers, lenders or debenture holders having floating charge. Where a receiver is appointed on behalf of the holders of any debentures or possession is taken by or on behalf of those debenture holders of any property subject to charge then payment made in respect of such debt shall, be recouped, as far as may be out of the assets available for payment of unsecured creditors (section 123).

#### Answer 5(b)

The salient features of the Limited Liability Partnership are as follows:

- (1) The LLP is a body corporate and a legal entity separate from its partners. Any two or more persons, associated for carrying on a lawful business with a view to earn profit, may by subscribing their names to an incorporation document and filing the same with the Registrar, form a Limited Liability Partnership. The LLP will have perpetual succession.
- (2) The mutual rights and duties of partners of an LLP interse and those of the LLP

and its partners shall be governed by an agreement between partners or between the LLP and the partners subject to the provisions of the legislation. There would be flexibility to devise the agreement as per their choice. In the absence of any such agreement the mutual rights or duties shall be governed by the provisions of the legislation.

- (3) The LLP will be a legal entity, liable to the full extent of its assets with the liability of the partners being limited to their agreed contribution in the LLP which may be tangible or intangible in nature or both tangible or intangible in nature. No partner would be liable on account of the independent or unauthorized acts of other partners or their misconduct.
- (4) Every LLP shall have at least two partners or shall also have at least two individuals as designated partners of whom at least one shall be resident in India. The duties and obligations of designated partners shall be as provided in the law.
- (5) The LLP shall be under an obligation to maintain annual accounts reflecting true and fair view of its state of affairs. A statement of accounts and solvency shall be filed by every LLP with the Registrar every year. The accounts of LLPs shall also be audited, subjected to any class of LLPs being exempted from this requirement by the Central Government.
- (6) The Central Government shall have powers to investigate the affairs of an LLP, if required by appointment of competent inspector for the purpose.
- (7) The Indian Partnership Act, 1932 shall not be applicable to LLPs. Other entities may convert themselves to LLP in accordance with the provisions of the legislation.
- (8) The Central Government has framed rules for carrying out the provisions of the proposed legislation.

#### Question 6

- (a) *State, giving reasons in brief, whether the following statements are correct or incorrect :*
  - (i) *Auditor of a government company is appointed or re-appointed by the Central Government on the advice of Comptroller and Auditor General of India (CAG).*
  - (ii) *Joint-holders of shares in a public company are not a single member.*
  - (iii) *In case of forged, illegal or void ab-initio transactions, the doctrine of 'indoor management' protects an outsider.*
  - (iv) *DIN is a unique identification number and once obtained is valid for life time of a director.* (2 marks each)
- (b) *List out the various registers required to be maintained statutorily under the Companies Act, 1956.* (8 marks)

#### Answer 6(a)(i)

*The statement is not correct.* Section 619(2) of the Companies Act, 1956 provides that the auditor of a Government company shall be appointed or re-appointed by the Comptroller and Auditor General of India (C&AG).



Earlier, such auditors were appointed or re-appointed by the Central Government on the advice of Comptroller and Auditor General of India (C&AG).

**Answer 6(a)(ii)**

*The statement is correct.* Joint holders of shares in a public company are not a single member. Each of the joint holders of shares is a member of the company but joint holders are counted as one member for the purpose of determining the maximum number of members i.e. fifty in a private company and for determining quorum at general meetings and for the purpose of determining members required for making applications under Sections 397 and 398 of the Companies Act, 1956 etc.

**Answer 6(a)(iii)**

*The statement is not correct.* The doctrine of indoor management does not extend to transactions involving forgery or to transactions which are otherwise void or illegal ab initio. It does not protect an outsider. Because, in the case of forgery it is not that there is absence of free consent but there is no consent at all. The person whose signatures have been forged is not even aware of the transaction and the question of his consent being free or otherwise does not arise. Consequently, it is not that the title of the person is defective but there is no title at all. Therefore, howsoever clever the forgery might have been the personator acquires no rights at all.

**Answer 6(a)(iv)**

*The statement is correct.* DIN is a unique identification number and once obtained is valid for life time of a director.

All existing directors and any person intending to be appointed as a director are required to obtain the Director Identification Number (DIN). DIN is also mandatory for directors of Indian Companies who are not citizens of India. However, DIN is not mandatory for directors of foreign company having branch offices in India. Only a single DIN is required for an Individual irrespective of number of directorships held by him.

**Answer 6(b)**

Every company incorporated under the Act is required to keep at its registered office, inter alia, the following statutory books and registers –

1. Register of investments in securities not held in company's name.[Section 49(7)]
2. Register of deposits. [Section 58A and the Companies (Acceptance of Deposits) Rules, 1975 and the RBI Non Banking Financial Companies Directions]
3. Register of securities bought back. (Section 77A)
4. Register of charges. (Section 143)
5. Register and index of members. [Sections 150, 151 and the Companies (Issue of Share Capital with Differential Voting Rights) Rules, 2001]
6. Register and index of debenture holders. (Section 152)
7. Register and index of beneficial owners. (Section 152A)
8. Foreign register of members and debenture holders and their duplicates. [Section 157(1) and 158(4)]

9. Copies of Annual Return (Section 163)
10. Books containing minutes of meetings of general, Board and committees of Directors. [Section 193(1)]
11. Register of Postal Ballot [the Companies (Passing of the resolutions by postal ballot) Rules, 2001]
12. Books of accounts. [Section 209(1)(a) to (c)]
13. Cost account records for Companies engaged in industries so specified by Central Government [Section 209(1)(d)]
14. Register of contracts with companies/firms in which directors are interested. [Section 301(5)]
15. Register of Directors/Managing Directors/Managers/Whole-time Directors/Secretary. (Section 303)
16. Register of directors' shareholdings. (Section 307)
17. Register of loans or investments made, guarantees given and security provided to other body corporate. (Section 372A)
18. Register of Renewed and Duplicate Share Certificates. [Rule 7 of the Companies (Issue of Share Certificate) Rules, 1960]
19. Register of records and documents destroyed [Section 163 and the Companies (Preservation and Disposal of Records) Rules, 1966]
20. Register of sweat equity shares [Section 79A and the Unlisted Companies (Issue of Sweat Equity Shares) Rules, 2003]
21. Dividend Register

#### Question 7

- (a) Briefly explain the various modes of winding-up of a company. (8 marks)
- (b) Briefly explain the following terms used under e-filing —
- (i) Pre-fill
  - (ii) Attachment
  - (iii) Check form
  - (iv) Pre-scrutiny. (2 marks each)

#### Answer 7(a)

A company registered under the Companies Act, 1956 may be wound up in any of the following modes:

1. By the Court i.e. compulsory winding up;
2. Voluntary winding up, which may be either:
  - (a) Members' voluntary winding up; or
  - (b) Creditor's voluntary winding up;
3. Winding up subject to the supervision of the Court.

Winding up by the Court or compulsory winding up is initiated by an application by way of petition to the appropriate Court for a winding up order.

In a member's voluntary winding up, when the company is solvent and is able to pay its liabilities in full, it need not consult the creditors or call their meeting. Its directors, or where they are more than two, the majority of its directors may, at a meeting of the Board, make a declaration of solvency verified by an affidavit stating that they have made full enquiry into the affairs of the company and that having done so they have formed an opinion that the company has no debts or that it will be able to pay its debts in full within such period not exceeding three years from the commencement of the winding up as may be specified in the declaration.

Where a declaration of solvency of the company is not made and delivered to the Registrar in a voluntary winding up, it is a case of creditor's voluntary winding up.

When a company has by special or ordinary resolution resolved to wind up voluntarily, the Court may make an order that the voluntary winding up shall continue, but subject to such supervision of the Court and with such liberty for creditors, contributories or others to apply to the Court and generally on such terms and conditions, as the Court thinks just (Section 522 of the Companies Act, 1956).

#### **Answer 7(b)(i)**

##### **Pre-fill**

Pre-fill is functionality in an e-Form that is used for filling automatically, the requisite data from the system without repeatedly entering the same. For example, by entering the CIN of the company, the name and registered office address of the company shall automatically be pre-filled by the system without any fresh entry.

#### **Answer 7(b)(ii)**

##### **Attachment**

An attachment refers to a document that is sent as an enclosure with an e-Form by means of an attached file. The objective of the attachment is to provide details relevant to the e-Form for processing. While some attachments are optional some are mandatory in nature.

The attachments to an e-Form has to in Adobe PDF format only. My MCA portal does not accept big attachment and the user is advised to keep the attachment size to minimum.

If the size of e-Form including attachment is more than the prescribed limit then the attachment may be filed through an addendum. In such cases, the details may be submitted in a floppy or compact disc at the ROC office.

#### **Answer 7(b)(iii)**

##### **Check Form**

By clicking "Check Form", the user will be in a position to find out whether the mandatory fields in an e-Form are duly filled-in. For example, if the user enters alphabets in "Date of Appointment of Director" field, he/she will be asked to correct that.

**Answer 7(b)(iv)****Pre-Scrutiny**

Pre-scrutiny is a functionality that is used for checking whether certain core aspects are properly filled in the e-Form. The user has to make the necessary attachments in PDF format before submitting the e-Form for pre-scrutiny.

**Question 8**

- (a) *A managing director of a company stood as surety for the repayment of loan taken by it for which he was paid guarantee commission. Does this commission amount to managerial remuneration? Support your answer with decided case law, if any. (5 marks)*
- (b) *A whole-time director of a company made an invention during the course of his employment with the company. He patented the invention in his own name and appropriated the benefits to himself. Can he do so? Cite case law, if any. (5 marks)*
- (c) *Articles of association of a company reserved the powers for calling the annual general meeting. The managing director of the company, without reference to the Board, called an annual general meeting. Is the annual general meeting validly called? If not, what should be done to make it valid? Discuss with reference to case law, if any. (6 marks)*

**Answer 8(a)**

Guarantee commission paid to directors for giving surety against loans on credit facilities availed by the company from financial institutions is not a remuneration for any professional services within the meaning of section 309 of the Companies Act, 1956. The director giving guarantee does not render any clerical, technical or administrative services to the company. He gets the commission for the risk undertaken which is his personal liability and nothing to do with his directorship. [*Suessen Textile Bearings Ltd. v. Union of India* [1984] 55 Co mp. Cas 492 (Delhi)].

Therefore, in view of the above case law, guarantee commission paid to managing director of a company will not amount to managerial remuneration.

**Answer 8(b)**

The directors are liable to the company for all personal profits or gain made by them taking advantage of their position as directors.

A director was held liable when a director patented and exploited in his own name an invention made during the course of his employment with the company [*Cranleigh Precision Engineering Ltd. v. Bryan*, (1964) All ER 289].

Therefore, the whole time director can get the invention patented in his own name and appropriate the benefits to him but he is liable to the company for all the personal gains he made with the help of the patented invention.

**Answer 8(c)**

Subject to the provisions in the articles, any general meeting of the company can be called only on the authority of a Board resolution. If the managing director, manager,

secretary or other officer calls a meeting without the authority of the Board of directors it will not be effectual unless the Board ratifies the convening of the general meeting before it is held. [*Re. Haycraft Gold Reduction and Mining Co.*, (1900) 2 Ch 230]. Also refer *British Asbestos Co. Ltd. v. Boyd*. (1903) 2 Ch 439.

Therefore, in the present case, managing director can validly call an annual general meeting (AGM) without referring to the Board only if the Board ratifies the convening of AGM before the meeting is held.

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## ECONOMIC AND LABOUR LAWS

Time allowed : 3 hours

Maximum marks : 100

### PART A

(Answer Question No.1 which is compulsory  
and any three of the rest from this part.)

#### Question 1

With reference to the relevant legal enactments, write short notes on any five of the following :

- (i) Deficiency in service
- (ii) Exempted categories under the importer-exporter code (IEC) number
- (iii) Know your customer (KYC) guidelines
- (iv) Anti-competitive agreements
- (v) Minimum resale price maintenance
- (vi) Contents of complete specification
- (vii) Principal display panel. (3 marks each)

#### Answer 1(i)

##### Deficiency in Service

According to Section 2(1)(g) of the Consumer Protection Act, 1986 deficiency means any fault, imperfection, shortcoming or inadequacy in the quality, nature and manner of performance which is required to be maintained by or under any law for the time being in force or has been undertaken to be performed by a person in pursuance of a contract or otherwise in relation to any service.

Examples of Deficiency in Service:

- Failure to maintain the quality of performance required by the law or failure to provide services as per warranties given, by the provider of the service would amount to 'deficiency in service'.
- Default or negligence in regard to settlement of an insurance claim would constitute a deficiency of service on the part of insurance company.

#### Answer 1(ii)

##### Exempted Categories under the importer exporter code (IEC) Number

The following categories of importers or exporters have been exempted from obtaining IEC number:

- (i) Ministries/Departments of the Central or State Government.
- (ii) Persons importing or exporting goods for personal use not connected with trade or manufacture or agriculture.

- (iii) Persons importing/exporting goods from/to Nepal provided the CIF value of a single consignment does not exceed Indian Rs. 25,000.
- (iv) Persons importing/exporting goods from/to Myanmar through Indo-Myanmar border areas provided the CIF value of a single consignment does not exceed Indian Rs. 25,000.
- (v) Importers covered by clause 3(1) [except sub-clauses (e) and (l)] and exporters covered by clause 3(2) [except sub-clauses (i) and (k)] of the Foreign Trade (Exemption from application of Rules in certain cases) Order, 1993.

**Answer 1(iii)****'Know Your Customer' (KYC) Guidelines**

In terms of the guidelines issued by the Reserve Bank of India (RBI) on *Know Your Customer [KYC] Standards – Anti Money Laundering [AML] Measures*, all banks are required to put in place a comprehensive policy framework covering KYC Standards and AML Measures. RBI introduced KYC guidelines for all banks.

KYC enables banks to know/ understand their customers and their financial dealings to be able to serve them better and manage its risks prudently.

The objective of KYC guidelines is to prevent banks from being used, intentionally or unintentionally, by criminal elements for money laundering activities. KYC procedures also enable banks to know/understand their customers and their financial dealings better which in turn help them manage their risks prudently. Banks should frame their KYC policies incorporating the following four key elements:

- (i) Customer Acceptance Policy;
- (ii) Customer Identification Procedures;
- (iii) Monitoring of Transactions; and
- (iv) Risk management.

**Answer 1(iv)****Anti Competitive Agreements**

It is provided under Section 3(1) of the Competition Act, 2002 that no enterprise or association of enterprises or person or association of persons shall enter into any agreement in respect of production, supply, distribution, storage, acquisition or control of goods or provision of services, which causes or is likely to cause an appreciable adverse effect on competition.

Section 3(2) further declares that any anti competitive agreement within the meaning of sub-section 3(1) shall be void. Under the law, the whole agreement is construed as 'void' if it contains anti-competitive clauses having appreciable adverse effect on competition.

Section 3(3) provides that following kinds of agreements entered into between enterprises or association of enterprises or persons or association of persons or person or enterprise or practice carried on, or decision taken by any association of enterprises

or association of persons, including “cartels”, engaged in identical or similar goods or services which –

- (a) directly or indirectly determines purchase or sale prices;
- (b) limits or controls production, supply, markets, technical development, investment or provision of services;
- (c) shares the market or source of production or provision of services by way of allocation of geographical area of market, or type of goods or services, or number of customers in the market or any other similar way; and
- (d) directly or indirectly results in bid rigging or collusive bidding;

shall be presumed to have an appreciable adverse effect on the competition.

Section 3(4) provides that any agreement amongst enterprises or persons at different stages or levels of the production chain in different markets, in respect of production, supply, distribution, storage, sale or price of, or trade in goods or provision of services, including :

- (a) tie-in agreement;
- (b) exclusive supply agreement;
- (c) exclusive distribution agreement;
- (d) refusal to deal;
- (e) resale price maintenance;

shall be an agreement in contravention of sub-section (1) if such agreement causes or is likely to cause an appreciable adverse effect on competition in India.

### **Answer 1(v)**

#### **Minimum resale price maintenance**

Minimum resale price is prohibited under Sections 39 and 40 of the MRTP Act, 1969. Section 39(1) provides that any term or condition of a contract for the sale of goods by a person to a wholesaler or retailer or any agreement between a person and wholesaler or retailer relating to such sale shall be void in so far as it purports to establish or provide for the establishment of minimum prices to be charged on the resale of goods in India.

It is only that portion in the agreement which contains provision for minimum resale price maintenance which would be void. The rest of the agreement would not be affected by this provision.

Not only minimum resale price maintenance is statutorily declared void and unenforceable at law, it also gives rise to criminal liabilities and is punishable with imprisonment or fine or both under Section 51 of the Act.

Section 41 empowers the Commission to exempt particular classes of goods from the provisions of minimum resale price maintenance contained Section 39 and 40.



**Answer 1(vi)****Contents of Complete Specification**

Section 10 of the Patents Act, 1970 dealing with contents of Specifications provides that every specification, whether provisional or complete, shall describe the invention and begin with a title sufficiently indicating the subject matter to which the invention relates. Every complete specification is required to -

- (a) fully and particularly describe the invention and its operation or use and the method by which it is to be performed;
- (b) disclose the best method of performing the invention which is known to the applicant and for which he is entitled to claim protection;
- (c) end with a claim or claims defining the scope of the invention for which protection is claimed; and
- (d) be accompanied by an abstract to provide technical information on the invention.

**Answer 1(vii)****Principal Display Panel**

'Principal display panel', in relation to a package, has been defined under section 2(w) of the Standard Weight and Measure Act, 1976 to mean the total surface area of the package where the information is required to be given. All the information could be grouped together and given in one place; or the pre-printed information could be grouped together and given in one place and online information group together in other place.

Rule 7 of the Standard Weight and Measure (Package Commodities) Rule 1977 specifies the area, size, letter, etc. of the principal display panel in different cases. In case of a package having a capacity of five cubic centimeters or less, the principal display panel may be card or tape affixed firmly to the package or container or bearing the required information.

Rule 7(4) provides that the height of any numeral in the declaration on the principal display package should not be less than that specified in Table I to this rule.

**Question 2**

*State, giving reasons in brief, whether the following statements are true or false. Attempt any five :*

- (i) *In case an EOU fails to achieve its export obligations, it shall be liable to pay penalty at the time of exit.*
- (ii) *A person resident outside India can sell the shares and convertible debentures of an Indian company to whomsoever he wants.*
- (iii) *'Goods' means every kind of movable property other than actionable claims and includes stock and shares even before allotment.*
- (iv) *Tea is a 'food stuff' and hence constitutes an essential commodity under the Essential Commodities Act, 1955.*

- (v) *An association pursuing a definite cultural, economic, educational, religious or social programme can receive foreign contribution without any limits.*
- (vi) *The provisions contained in the Special Economic Zones Act, 2005 shall have effect notwithstanding anything inconsistent therewith contained in any other law for the time being in force.* (3 marks each)

**Answer 2(i)****True**

*Reasons* : According to Foreign Trade Policy, the EOU units may, with the prior approval of the Development Commissioner, opt out of the scheme, subject however to payment of Excise and customs duties and in terms of the industrial policy in force at the time of exit. In case the unit has not achieved the export obligations, it shall also be liable to penalty at the time of exit from EOU Scheme.

**Answer 2(ii)****False**

*Reasons* : As per Regulation 9 of FEM (Transfer or Issues of Security by a person Resident outside India) Regulations, 2000 a person resident outside India (Other than NRI) may transfer by way of sale or gift the shares or convertible debentures to any person resident outside India (including NRIs).

A person resident outside India can sell the shares and convertible debentures of an Indian company on a recognized Stock Exchange in India through a registered broker.

**Answer 2(iii)****False**

*Reasons* : Goods, in terms of Section 2(1)(i) of the Consumer Protection Act, 1986 to mean goods as defined in the Sale of Goods Act, 1930. As per Section 2(7) of the Sale of Goods Act, 1930 Goods means every kind of movable property other than actionable claims and money; and includes stock and shares, growing crops, grass and things attached to or forming part of the land, which are agreed to be severed before sale or under the contract of sale.

In *Morgan Stanley Mutual Fund v. Kartik Das* (1994) 3 CLJ 27, the Supreme Court held that an application for allotment of shares cannot constitute goods. It is after allotment, rights may arise as per the articles of association of the company.

**Answer 2(iv)****False**

*Reasons* : In *S. Samuel, AID. Harrison's Malayava v. Union of India*, AIR 2004 SC 218, Supreme Court held that Tea is not foodstuff. Even in a wider sense, foodstuffs will not include tea as tea either in the form of the leaves or in the form of beverage, does not go into the preparation of food proper to make it more palatable and digestible.

In common parlance, any one who has taken tea would not say that he has taken or eaten food. Thus tea is not a food.

**Answer 2(v)****True**

*Reason* : Under Section 6 of the Foreign Contribution Regulation Act, 1976 associations having a definite cultural, economic, educational, religious or social programme, receipt of foreign contribution by any such association is permitted only if it registers itself with the Central Government in accordance with the Foreign Contribution (Regulation) Rules. Moreover, every such association is required, within the prescribed time and manner to give an intimation to the Central Government regarding:

- (a) amount of foreign contribution received;
- (b) source of such foreign contribution;
- (c) manner in which such contribution was received;
- (d) purpose for which such contribution was utilised;
- (e) the manner in which such contribution was utilised.

**Answer 2(vi)****True**

*Reason* : Special Economic Zones Act, 2005 has been given overriding effect. As per Section 51 the provisions of this Act shall have effect notwithstanding anything inconsistent therewith contained in any other law for the time being in force or in any instrument having effect by virtue of any law other than this Act.

**Question 3**

(a) *Distinguish between any two of the following :*

- (i) 'Seizure' and 'confiscation' under the Essential Commodities Act, 1955.
- (ii) 'COB licence' and 'industrial licence'.
- (iii) 'Invention' and 'patentable invention' under the Patents Act, 1970.

(5 marks each)

(b) *Choose the most appropriate answer from the given options in respect of the following :*

- (i) *Under the Consumer Protection Act, 1986, the limitation period for filing a complaint from the date of cause of action is —*
  - (a) 60 days
  - (b) 6 months
  - (c) 1 year
  - (d) 2 years.
- (ii) *The amount representing the full export value of goods is required to be realised and repatriated in India within —*
  - (a) 6 months
  - (b) 3 months

- (c) 1 year
- (d) 2 years.
- (iii) *The issue of Foreign Currency Convertible Bonds (FCCBs) in any financial year is subject to a ceiling of —*
  - (a) *Rs.50 crore*
  - (b) *US \$500 million*
  - (c) *Rs.100 crore*
  - (d) *US \$1 million.*
- (iv) *A registered trade mark requires to be renewed on expiry of the period of —*
  - (a) *7 years*
  - (b) *10 years*
  - (c) *14 years*
  - (d) *5 years.*
- (v) *Foreign direct investment (FDI) is prohibited in —*
  - (a) *Infrastructure sector*
  - (b) *Hospitals*
  - (c) *Retail trade*
  - (d) *IT sector.*

(1 mark each)

### **Answer 3(a)(i)**

The general distinction between confiscation and seizure, in the context of the Essential Commodities Act, is that an essential commodity which has been seized could be confiscated. Therefore, confiscation is an action posterior to the seizure of the essential commodity.

A commodity that has not been seized cannot be confiscated. Seizure itself does not imply confiscation. The seizure should have been made by virtue of an order passed under Section 3 of the Essential Commodities Act, 1955.

Clause (j) of Section 3 empowers the Government to make an order for seizure of any essential commodity if an order made by the Central Government controlling production, supply, distribution etc. of essential commodities has been or is about to be contravened. Therefore, any contravention or intended contravention of an order passed by the Government under the Act may lead to seizure, and under the circumstances mentioned in Section 6A such seized commodity could be confiscated.

### **Answer 3(a)(ii)**

A COB licence is required when a small scale unit exceeds the prescribed small scale limit of investment in plant and machinery by way of natural growth and continues to manufacture small scale reserved items(s). Also, if exemption from Industrial licensing granted for any item is withdrawn, the industrial undertakings manufacturing such item(s) require COB licence.

An Industrial licence is a written permission from the Government to an industrial undertaking to manufacture specified articles, listed in the First Schedule and includes particulars of industrial undertaking, its location, articles to be manufactured, the capacity on the basis of maximum utilization of plant and machinery etc. The licence is subject to a validity period within which the licensed capacity of the undertaking should be established.

**Answer 3(a)(iii)**

Section 2(j) of the Patents Act, 1970 defines the term invention as to mean a new product or process involving an inventive step and capable of Industrial application.

The term ‘inventive step’ means a feature of an invention that involves technical advance as compared to the existing knowledge or having economic significance or both that makes the invention not obvious to a person skilled in the art.

Patentable invention is an invention relating either to a product or process that is new, involving inventive step and capable of industrial application can be patented. However it must not fall in to the categories of inventions that are non-patentable under section 3 and 4 of the Patents Act, 1970.

**Answer 3(b)(i)**

(d) 2 years

**Answer 3(b)(ii)**

(c) 1 year

**Answer 3(b)(iii)**

(b) US\$500 million

**Answer 3(b)(iv)**

(b) 10 years

**Answer 3(b)(v)**

(c) Retail trade.

**Question 4**

(a) *What are the circumstances under which a registered trade mark is deemed to be infringed under the Trade Marks Act, 1999. (5 marks)*

(b) *Write a note on global initiatives in the prevention of money laundering. (5 marks)*

(c) *The insured (since deceased) had taken out four life policies with double accident benefits, premium payable half-yearly. When the third premium fell due, an agent of the insurer met the insured and took a bearer cheque towards the premium payable by him in respect of the policies. Although, the cheque was encashed immediately, it was not deposited with the insurer for 3 months. In the meantime, the insured met with a fatal accident and died. The widow filed a claim for payment of the sum assured. The insurer pleaded that the insurance agent had no implied authority to collect the premium. Will the widow succeed in her claim ? (5 marks)*

**Answer 4(a)**

Section 29 of the Trade Marks Act, 1999 dealing with infringement of trade marks, explicitly enumerates the grounds which constitute infringement of a trademark. This section lays down that when a registered trade mark is used by a person who is not entitled to use such a trade mark under the law, it constitutes infringement. This section clearly states that a registered trade mark is infringed, if

- (a) the mark is identical and is used in respect of similar goods or services; or
- (b) the mark is similar to the registered trade mark and there is an identity or similarity of the goods or services covered by the trade mark; or
- (c) the trade mark is identical and is used in relation to identical goods or services;

and that such use is likely to cause confusion on the part of the public or is likely to be taken to have an association with the registered trade mark.

**Answer 4(b)****Prevention of Money Laundering – Global Initiatives**

Since money laundering is an international phenomenon, transnational co-operation is of critical importance in the fight against this menace. A number of initiatives have been taken to deal with the problem at international level. In this context, the United Nations or the Bank for International Settlements, took some initiatives in 1980s to address the problem of money laundering. However, with the creation of the Financial Action Task Force (FATF) in 1989, regional groupings, such as the European Union, Council of Europe, and organisation of American States also established anti- money laundering standards for their member countries.

The major international agreements addressing money laundering include the United Nations Convention against Illicit Trafficking in Drugs and Psychotropic Substances (the Vienna Convention) and Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds of Crime.

The role of financial institutions in preventing and detecting money laundering has also been the subject of pronouncements by the Basle Committee on Banking Regulation Supervisory Practices, the European Union and the International Organization of Securities Commissions.

**Answer 4(c)**

The facts of the case are similar to that of *Harshad J. Shah v. Life Insurance Corporation of India* [1997(3) SCALE 423 (SC)] the Supreme Court held that the agent had no express authority to receive the premium on behalf of the Corporation. In his letter of appointment there was a condition expressly prohibiting him from collecting the premium. Nor could it be said that he had an implied authority to collect the premium, as regulation 8(4) of LIC of India (Agent) Regulation expressly prohibited the agents from collecting premium. In the facts of this case there was no room to invoke the doctrine of apparent authority underlying Section 237 of the Indian Contract Act.

In this case Supreme Court order for the amount of premium with interest and the costs to be paid to the widow.

**Question 5**

- (a) *What are the restrictions on the acceptance of foreign contribution by organisations of political nature under the Foreign Contributions (Regulation) Act, 1976 ?* (5 marks)
- (b) *Write a note on regulatory framework for environmental protection in India.* (5 marks)
- (c) *With reference to the relevant provisions of the Foreign Exchange Management Act, 1999 and the rules and regulations made thereunder, advise on the following:*
- (i) *ABC Ltd., a company listed on the National Stock Exchange Ltd., is interested in investing in a company in the USA.*
  - (ii) *Ram, an NRI resident in Nepal, is interested to invest in shares and convertible debentures of an Indian company.*
  - (iii) *A foreign investor wants to invest in an Indian company which is a small scale industrial unit.*
  - (iv) *Brown, a UK citizen, is interested to make investment in the form of foreign direct investment (FDI) in retail trading business.*
  - (v) *XYZ Ltd., a company listed on the Bombay Stock Exchange Ltd., wants to issue shares under the Employees Stock Option Scheme (ESOP) to the employees of its joint venture abroad.* (1 mark each)

**Answer 5(a)**

Section 5 of Foreign Contribution Regulation Act, 1976 prohibits an organisation of a political nature not being a political party, from accepting any foreign contribution, except with the prior permission of the Central Government. In this context, it has been clarified that an organisation of a political nature not being a political party means such organisation as the Central Government may specify by order published in the Official Gazette, having regard to the activities of the organisation or the ideology propagated by the organisation or the programme of the organisation or the association of the organisation with the activities of any political party.

No person resident in India and no citizen resident outside India is allowed to accept without the previous permission of the Central Government, any foreign contribution or acquire or agree to acquire any foreign currency on behalf of an organisation of political nature, not being a political party. Section 5 further prohibits a person resident in India to deliver, without the prior permission of the Central Government, any foreign currency to any person if he knows or has reasonable cause to believe that such other person intends, or is likely, to deliver such currency to an organisation of political nature. A citizen of India, resident outside India, has also been prohibited from delivering any currency, whether Indian or foreign, which has been accepted from any foreign source to an organisation of a political nature or any person, if he knows or has reasonable cause to believe that such person intends or is likely to deliver such currency to an organisation of a political nature.

It may be noted that for the purposes of Section 5, the Central Government has notified certain organisations as organisations of political nature, not being a political party.

**Answer 5(b)**

In India, as in other developing countries, the environmental problems are not confined to side effects of industrialisation but reflect the inadequacy of resources to provide infrastructural facilities to prevent industrial pollution.

Though the Indian Penal Code, 1860 contains penal provisions for corrupting or fouling the water or spring or reservoir so as to make it less fit for the purpose for which it is ordinarily used as well as for vitiating the atmosphere so as to make it noxious to the health of any person etc. A number of other Central and State laws covering boilers, dangerous drugs, radiation, forests, etc. were enacted during the middle of the 20th century, however the legislative and administrative measures directed specifically at protection of the environment were introduced in the 1970s and 1980s are as under :

- (i) The Water (Prevention and Control of Pollution) Act, 1974
- (ii) The Air (Prevention and Control of Pollution) Act 1981.
- (iii) Environment (Protection) Act, 1986
- (iv) Public Liability Insurance Act, 1991
- (v) The National Environment Tribunal Act, 1995
- (vi) The National Environment Appellate Authority Act, 1997.

**Answer 5(c)(i)**

Listed Indian companies are permitted to invest up to 50 per cent of their net worth as on the date of the last audited balance sheet in (i) shares, and (ii) bonds/fixed income securities, rated not below investment grade by accredited/ registered credit rating agencies, issued by listed overseas companies.

In the light of the above provision, ABC Ltd. can invest in a company in the USA.

**Answer 5(c)(ii)**

NRIs resident in Nepal and Bhutan as well as citizens of Nepal and Bhutan are permitted to invest in shares and convertible debentures of Indian companies under FDI Scheme on repatriation basis, subject to the condition that the amount of consideration for such investment shall be paid only by way of inward remittance in free foreign exchange through normal banking channels or by debit to the NRE/ FCNR (B) accounts of the NRIs.

In the light of the above, Ram a NRIs can invest in shares and convertible debentures of an Indian company.

**Answer 5(c)(iii)**

A foreign investor can invest in an Indian company which is a small scale industrial unit provided it is not engaged in any activity which is prohibited under the FDI policy. Such investments are subject to a limit of 24% of paid-up capital of the Indian company/ SSI Unit. However, an SSI Unit can issue equity shares/fully convertible preference shares / fully convertible debentures more than 24% of its paid-up capital if:

- (a) It has given up its small scale status,



- (b) It is not engaged or does not propose to engage in manufacture of items reserved for small scale sector, and
- (c) It complies with the sectoral caps.

**Answer 5(c)(iv)**

As per Foreign Direct Investment policy, foreign investment in any form is prohibited in a company or a partnership firm or a proprietary concern or any entity, whether incorporated or not (such as Trusts) which is engaged or propose to engage in retail trading business (except single brand product retailing).

In the light of the above provision, Brown can not invest in retail trading business (except single brand product retailing).

**Answer 5(c)(v)**

XYZ Limited can issue shares under the Employees Stock Option Scheme (ESOPs), to its employees or employees of its joint venture or wholly owned subsidiary abroad, other than citizens of Pakistan. Shares under ESOPs can be issued directly or through a Trust subject to the condition that:

- (i) The scheme has been drawn in terms of relevant regulations issued by the Securities and Exchange Board of India; and
- (ii) The face value of the shares to be allotted under the scheme to the non-resident employees does not exceed 5 per cent of the paid-up capital of the issuing company.

**PART B**

*(Answer ANY TWO questions from this part.)*

**Question 6**

*Write notes on any four of the following :*

- (i) *'Dependent' under the Employees' State Insurance Act, 1948.*
- (ii) *'Methods of fixing and revising minimum rates of wages' under the Minimum Wages Act, 1948.*
- (iii) *Object and scope of the Payment of Bonus Act, 1965.*
- (iv) *'Obligations of the principal employer' under the Contract Labour (Regulation and Abolition) Act, 1970.*
- (v) *Principles laid down by the Supreme Court with regard to retrenchment under the Industrial Disputes Act, 1947.*
- (vi) *'Occupier' under the Factories Act, 1948.* *(5 marks each)*

**Answer 6(i)****Dependent under the ESI Act, 1948**

"Dependent" under Section 2(6A) of the ESI Act, 1948 means any of the following relatives of a deceased insured person namely:

- (i) a widow, a minor legitimate or adopted son, an unmarried legitimate or adopted daughter,

- (ia) a widowed mother,
- (ii) if wholly dependent on the earnings of the insured person at the time of his death, a legitimate or adopted son or daughter who has attained the age of 18 years and is infirm;
- (iii) if wholly or in part dependent on the earnings of the insured person at the time of his death:
  - (a) a parent other than a widowed mother,
  - (b) a minor illegitimate son, an unmarried illegitimate daughter or a daughter legitimate or adopted or illegitimate if married and minor or if widowed and a minor,
  - (c) a minor brother or an unmarried sister or a widowed sister if a minor,
  - (d) a widowed daughter-in-law,
  - (e) a minor child of a pre-deceased son,
  - (f) a minor child of a pre-deceased daughter where no parent of the child is alive or,
  - (g) a paternal grand parent if no parent of the insured person is alive.

#### **Answer 6(ii)**

#### **Methods of Fixing and Revising Minimum Rates of Wages**

In fixing minimum rates of wages in respect of any scheduled employment for the first time or in revising minimum rates of wages so fixed, the appropriate Government shall follow either of the two methods specified under Section 5 of the Minimum Wages Act, 1948. These are as follows:

##### *Method One – Appointment of Committee*

This method is known as the 'Committee Method'. The appropriate Government may appoint as many committees and sub-committees as it considers necessary to hold enquiries and advise it in respect of such fixation or revision as the case may be. After considering the advice of the committee or committees, the appropriate Government shall, by notification in the Official Gazette fix or revise the minimum rates of wages in respect of each scheduled employment. The fixation or revision shall come into force on the expiry of three months from the date of the issue of notification unless the notification otherwise provides. [Section 5(1)(a)]

##### *Method Two- Notification of Proposal in the official Gazettee*

The method is known as the 'Notification Method'. While fixing minimum wages under Section 5(1)(b), the appropriate Government shall by notification, in the Official Gazette publish its proposals for the information of persons likely to be affected thereby and specify a date not less than 2 months from the date of notification, on which the proposals will be taken into consideration. [Section 5(1)(b)]

After considering the advice of the committee or committees (i.e. method one) or all

representations received by it before the date specified in the notification (i.e. method two), the appropriate Government shall, by notification in the Official Gazette fix or revise the minimum rates of wages in respect of each scheduled employment. The fixation or revision shall come into force on the expiry of three months from the date of its issue, unless the notification otherwise provides. Where the appropriate Government proposes to revise the minimum rate of wages by method –second, it shall consult the Advisory Board (constituted under Section 7 of the Act) also.

### **Answer 6(iii)**

#### **Object and Scope of the Payment of Bonus Act, 1965**

The object of the Payment of Bonus Act, 1965 is to provide for the payment of bonus to persons employed in certain establishments and for matters connected therewith. The Supreme Court has explained the object of the Payment of Bonus Act, 1965 in *Jalan Trading Co. (Pvt.) Ltd. v. Mill Mazdor Sabha*, AIR 1967 SC 691. Speaking through Justice Shah, the Apex Court observed that:

“ The object of the Act being to maintain peace and harmony between labour and capital by allowing the employees to share the prosperity of the establishment, and prescribing the maximum and minimum rates of bonus together with the scheme of “set-off” and “set on” not only secures the right of labour to share in the profits but also ensures a reasonable degree of uniformity”.

On the question whether the Act deals only with profit bonus, it was observed by the Supreme Court in *Mumbai Kamgar Sabha v. Abdulbhai Faizullabhai*, (1976) II LLJ 186, that “bonus” is a word of many generous connotations. There is profit based bonus which is one specific kind of claim and perhaps the most common. There is customary or traditional bonus which has its emergence from long, continued usage leading to a promissory and expectancy situation materialising in a right. There is attendance bonus and what not. The Bonus Act speak and speaks as a whole Code on the sole subject of profit based bonus but is silent and cannot, therefore, annihilate by implication, other distinct and different kinds of bonuses, such as the one oriented on custom. The Court held that a discerning and concrete analysis of the scheme of the Bonus Act and reasoning of the Court leaves no doubt that the Act leaves untouched customary bonus.

### **Answer 6(iv)**

#### **Obligations of the Principal Employer**

Under the Contract Labour (Regulation and Abolition) Act, 1970 a contractor is required to provide canteens, rest-rooms, latrines, urinals, drinking water, washing facilities and first aid facilities for the use of contract labour. (Sections 16-19)

If a contractor fails to provide the prescribed amenities, then the principal employer will be liable to provide such amenities. The principal employer can recover such expenses from the contractor. (Section 20)

Besides, the contractor is required to pay wages and a duty is cast on him to ensure disbursement of wages in the presence of the authorised representative of the principal employer. An obligation is also cast on the principal employer to nominate a representative duly authorised by him to be present at the time of disbursement of wages.

In case of failure on the part of the contractor to pay wages either in part or in full, the principal employer is liable to pay the same and recover the amount so paid from the contractor either by deduction from any amount payable to the contractor under any contract or as a debt payable by the contractor. (Section 21)

### **Answer 6(v)**

#### **Principles Laid Down by Supreme Court with Regard to Retrenchment**

The Industrial Disputes Act, 1947 defines retrenchment under Section 2(oo) as “the termination by the employer, of the service of the workman, for any reason, whatsoever, otherwise than as a punishment inflicted by way of disciplinary action but does not include voluntary retirement, compulsory retirement of the workman on reaching the age of superannuation or termination of service on the grounds of continued ill health.”

Thus, the definition contemplates following requirements for retrenchment:

- (i) There should be termination of the service of the workman.
- (ii) The termination should be by the employer.
- (iii) The termination is not the result of punishment inflicted by way of disciplinary action.
- (iv) The definition excludes termination of service on the specified grounds or instances mentioned in it.

The Supreme Court in the case of *Workmen of Subong Tea Estate v. Subong Tea Estate*, (1964) 1 L.L.J. 333, laid down the following principles with regard to retrenchment:

1. The management can retrench its employees only for proper reasons, which means that it must not be actuated by any motive of victimisation or any unfair labour practice.
2. It is for the management to decide the strength of its labour force, and the number of workmen required to carry out efficiently the work in his industrial undertaking must always be left to be determined by the management in its discretion.
3. If the number of employees exceeds the reasonable and legitimate needs of the undertaking, it is open to the management to retrench them.
4. Workmen may become surplus on the ground of rationalisation or on the ground of economy reasonably and bona fide adopted by the management or of other industrial or trade reasons.
5. The right of the employer to effect retrenchment cannot normally be challenged but when there is a dispute in regard to the validity of the retrenchment, it would be necessary for the tribunal to consider whether the impugned retrenchment was justified for proper reasons and it would not be open to the employer either capriciously or without any reason at all to say that it proposes to reduce its labour for no rhyme or reason.

**Answer 6(vi)****Occupier under the Factories Act, 1948**

Section 2(n) of the Factories Act, 1948 defines the term “occupier” as a person who has ultimate control over the affairs of the factory subject to the condition that-

- (i) in the case of a firm or other association of individuals, any one of the individual partners or members thereof shall be deemed to be the occupier;
- (ii) in the case of a company, any one of the directors, shall be deemed to be the occupier;
- (iii) in the case of a factory owned or controlled by the Central Government or any State Government, or any local authority, the person or persons appointed to manage the affairs of the factory by the Central Government, the State Government or the local authority, as the case may be, shall be deemed to be the occupier.

The important test whether a person is an occupier or not is the possession or vesting in of the ultimate control of the factory. An occupier may be an owner, a lessee or a mere licensee, but he must have the right to occupy the property and dictate terms of management.

There was a lot of controversy regarding ‘occupier in case of a company, as the Section 2(n)(ii) of the Factories Act provides that any one of the directors of the company shall be deemed to be occupier of the factory. The controversy was set at rest by the Supreme Court in the case of *J.K. Industries Ltd. v. Chief Inspector of Factories* (1997) I-L.L.J. SC 722, holding that only a member of Board of Directors of the Company can be occupier of the factory of the company. The ultimate control of factory owned by company vests in Board of Directors. Ultimate control which vests in Board of Directors cannot be vested in any one else. Company owing factory cannot nominate its employees or officers except director of the company as occupier of its factory.

**Question 7**

- (a) *Distinguish between any two of the following:*
  - (i) ‘Lay-off’ and ‘lock-out’ under the *Industrial Disputes Act, 1947*.
  - (ii) ‘Arbitration’ and ‘adjudication’ of disputes under the *Industrial Disputes Act, 1947*.
  - (iii) ‘Young person’ and ‘adult’ under the *Factories Act, 1948*. (5 marks each)
- (b) *Re-write the following sentences after filling-in the blank spaces with appropriate word(s)/figure(s) :*
  - (i) Minimum \_\_\_\_\_ years of contributory service is required for entitlement of pension under the *Employees’ Provident Funds and Miscellaneous Provisions Act, 1952*.
  - (ii) It is mandatory to register an establishment under the *Contract Labour (Regulation and Abolition) Act, 1970* in case it employs \_\_\_\_\_ labour through a contractor.

- (iii) A factory is required to appoint a welfare officer where \_\_\_\_\_ workers are ordinarily employed.
- (iv) The employer of an industrial establishment having 100 or more employees is required to submit draft standing orders within \_\_\_\_\_ months from the date on which the Industrial Employment (Standing Orders) Act, 1946 becomes applicable.
- (v) Contracting out of compensation by a workman under an agreement shall be \_\_\_\_\_. (1 mark each)
- (c) Choose the most appropriate answer from the given options in respect of the following.
- (i) The appropriate government shall revise the minimum rates of wages under the Minimum Wages Act, 1948 at least once in every —
- (a) 2 years
  - (b) 3 years
  - (c) 4 years
  - (d) 5 years.
- (ii) The disputes relating to benefits under the Employees' State Insurance Act, 1948 are required to be filed in —
- (a) Civil Court
  - (b) Employees' Insurance Court
  - (c) Labour Court
  - (d) Industrial Tribunal.
- (iii) An employee is entitled to receive bonus provided he has worked in an accounting year in the establishment for not less than —
- (a) 30 working days
  - (b) 1 year
  - (c) 8 months
  - (d) 4 months.
- (iv) An employer is not liable to pay compensation under the Workmen's Compensation Act, 1923, if the injury does not result in disablement for a period exceeding —
- (a) 1 week
  - (b) 3 days
  - (c) 1 month
  - (d) 6 months.
- (v) The Employees' Provident Funds and Miscellaneous Provisions Act, 1952 is applicable to commercial establishments employing —
- (a) 10 or more employees
  - (b) 20 or more employees
  - (c) 50 or more employees
  - (d) 100 or more employees. (1 mark each)

**Answer 7(a)(i)****Lay-off and lock-out**

- (1) In lay-off, the employer refuses to give employment due to certain specified reasons, but in lock-out, there is deliberate closure of the business and employer locks out the workers not due to any such reasons.
- (2) In lay-off, the business continues, but in lock-out, the place of business is closed down for the time being.
- (3) In a lock-out, there is no question of any wages or compensation being paid unless the lock-out is held to be unjustified.
- (4) Lay-off is the result of trade reasons but lock-out is a weapon of collective bargaining.
- (5) Lock-out is subject to certain restrictions and penalties but it is not so in case of lay-off.

However, both are of temporary nature and in both cases the contract of employment is not terminated but remains in suspended animation.

**Answer 7(a)(ii)****Arbitration and Adjudication**

Adjudication involves intervention in the dispute by the third party appointed by the government for the purpose of deciding the nature of final settlement. On getting a report of the failure of conciliation, the government has to decide whether it would be appropriate to refer the dispute to adjudication.

Arbitration is a procedure in which a dispute is submitted, by agreement of the parties, to one or more arbitrators who make a binding decision on the dispute. In choosing arbitration, the parties opt for a private dispute resolution procedure instead of going to court.

The circumstances under which an industrial dispute may be voluntarily referred to arbitration have been stipulated under Section 10A of the Industrial Disputes Act, 1947.

**Answer 7(a)(iii)****Young Person and Adult**

“Young Person” as per Section 2(d) of the Factories Act, 1948 means a person who is either a child or an adolescent.

“Adult” according to Section 2(a) of the Factories Act, means a person who has completed his eighteenth year of age.

**Answer 7(b)**

- (i) Minimum **10 years** of contributory service is required for entitlement of pension under the Employees’ Provident Funds and Miscellaneous Provisions Act, 1952.
- (ii) It is mandatory to register an establishment under the Contract Labour (Regulation

and Abolition) Act, 1970 in case it employs **20 or more** labour through a contractor.

- (iii) A factory is required to appoint a welfare officer where **500 or more** workers are ordinarily employed.
- (iv) The employer of an industrial establishment having 100 or more employees is required to submit draft standing orders within **6 months** from the date on which the Industrial Employment (Standing Orders) Act, 1946 becomes applicable.
- (v) Contracting out of compensation by a workman under an agreement shall be **null and void** .

**Answer 7(c)(i)**

- (d) 5 years

**Answer 7(c)(ii)**

- (b) Employees' Insurance Court

**Answer 7(c)(iii)**

- (a) 30 working days

**Answer 7(c)(iv)**

- (b) 3 days

**Answer 7(c)(v)**

- (b) 20 or more employees

**Question 8**

*Attempt any five of the following stating relevant legal provisions and decided case law, if any :*

- (i) *Muskan Theatre is maintaining a canteen and a cycle stand through private contractors. Regional Director, ESI Corporation sent notices to the management of the theatre for contribution of the employees engaged in the canteen and cycle stand. The management contends that they are not employees but are the workmen of the contractor. Hence, the management is not liable. Will the management succeed in its contention ?*
- (ii) *Rajat, a workman in a factory, had no vision in his left eye but the defect was not visible. Later, during welding operations, accidentally, a spark hit his blind eye. He lost his eye-ball and the blindness became visible. Though, there was no physical disability, he lost his employment because the defect became visible. Has the accident caused any disablement ? Is the employer liable to pay any compensation ?*
- (iii) *The workman of Bharat Chemicals went on go-slow strike to compel the management to concede to their demands. The management contended that go-slow is a serious misconduct and initiated disciplinary action against the erring workmen. Is the action of the management justified ?*
- (iv) *An employer failed to pay his contribution under the Employees' State Insurance*



*Act, 1948. After 6 years, the ESI Corporation issued a demand notice for payment of arrears of contribution. The employer contended that the arrears of contribution beyond 5 years are not recoverable. Will the employer succeed ?*

- (v) *Anil, a workman raised an industrial dispute contending that he was employed with effect from 1st April, 1986 on regular basis and his services were illegally terminated on 12th February, 1994. The employer took the stand that the workman was engaged on casual basis on daily wages for a specific period and for the specific work and that his services were not terminated on 12th February, 1994 but he had abandoned his job. The employer did not produce attendance record before the Labour Court and also failed to prove that the workman had worked for less than 240 days. The workman alleged violation of the provisions of the Industrial Disputes Act, 1947 relating to retrenchment. Will he succeed ?*
- (vi) *Ghee brought from various customers is sampled chemically, analysed and packed in tins for transportation to the head office of the company for sale in the market. Does it amount to manufacturing process under the Factories Act, 1948 ?*
- (vii) *Rohit lost his mental balance as a result of an injury by accident and committed suicide. Is the employer liable to pay compensation under the Workmen's Compensation Act, 1923 ?* (4 marks each)

#### **Answer 8(i)**

The management will not succeed in its contention. The theatre owner is liable to pay ESI contribution as principal employer.

On a similar issue in the case of *Royal Talkies Hyderabad v. ESI Corpn.*, AIR 1978 SC 1478, the Supreme Court held that if a contractor undertakes to run a canteen or a cycle stand in a theatre, he undertakes the execution of the whole or part of the work which is ordinarily part of the work of the theatre of the principal employer or is incidental to the purpose of the theatre. As such he comes within the definition of 'immediate employer' and the owner of the theatre within the definition of 'principal employer'. The theatre owner is liable for ESI contribution as principal employer of the workmen although they were engaged independently by the owner of the canteen or the cycle stand.

#### **Answer 8(ii)**

It is a case of total disablement.

"Total disablement" means, such disablement whether of a temporary or permanent nature, which incapacitates a workman for all work which he was capable of performing at the time of accident resulting in such disablement.

The expression incapacitates a workman for all work does not mean capacity to work or physical incapacity. In *Ball v. William Hunt & Sons Ltd.* 1912 A.C.496, it was held that if due to any physical defect, a workman is unable to get any work which a workman of his class ordinarily performs, and has thus lost the power to earn he is entitled to compensation for total disablement. It is immaterial that the workman is physically fit to perform some work.

**Answer 8(iii)**

The action of the management is justified. The act of go- slow of the workers amounts to misconduct. The legality of go-slow has been explained by the Supreme Court in the case of *Bharat Sugar Mills Ltd. v. Jai Singh*, (1961) 11 LLJ 644 (647) SC, in the following words

“Go-slow which is a picturesque description of deliberate delaying of production by workmen pretending to be engaged in the factory, is one of the most pernicious practices that discontented and disgruntled workmen sometimes resort to. Thus, while delaying production and thereby reducing the output, the workmen claim to have remained employed and entitled to full wages. Apart from this, ‘go-slow’ is likely to be much more harmful than total cessation of work by strike. During a go-slow much of the machinery is kept going on at a reduced speed which is often extremely damaging to the machinery parts. For all these reasons, ‘go-slow’ has always been considered a serious type of misconduct.”

**Answer 8(iv)**

The ESI Corporation can recover employer’s contribution even after lapse of five years. The Supreme Court in the case of *ESIC v. C.C. Santha Kumar* (JT 2006) (10) SC 549 has held that the limitation period of 5 years specified under section 77 of the ESI Act to bring an action before the Employees Insurance Court is not applicable in case of determination of the contribution payable under section 45A of the ESI Act, 1948. If the employer fails to challenge the determination made by the ESI Corporation under the provisions of section 45A or section 75 of the ESI Act, before the Employees’ Insurance Court, it becomes final against the employer. Therefore, the contention of the employer that the ESI Corporation cannot recover the dues pertaining to the period prior to five years, is not tenable in law.

**Answer 8(v)**

The materials on record clearly establish that the engagement of the workman was on casual basis on daily wages for specific period and for the specific work.

It has been held by the Supreme Court in a series of decisions that the burden of proof is on the workman to show that he had worked for 240 days in the preceding 12 calendar months prior to the alleged retrenchment. Further, presumption as to adverse inference for non production of muster-roll by the employer should not be taken as an inflexible rule. It is always optional, and one of the factors which is required to be taken into consideration is the background of the factors involved in the lis. [*Municipal Corpon. Faridabad v. Shri Niwas* (2004) 8 SCC 195; *Batala Co-op. Sugar Mills Ltd. v. Sowaran Singh*]

As stated above, the workman was on casual basis on daily wages for specific period and for the specific work. The termination of his services does not amount to retrenchment in view of section 2(oo)(bb) of the Industrial disputes Act. Hence, the contention of the workman that the management has violated section 25F of the Industrial disputes Act in terminating his services is devoid of merit. The workman will not succeed.

**Answer 8(vi)**

It is a manufacturing process. In the case of *Shri Laxmi Dass Premji Ghee Merchant v. R. Inspector of Factories Gantur* (1960) 1 LLJ, where ghee brought from various customers was sampled chemically, analysed and packed in tins for transportation to the Head Office of the concern for sale in the market, the court held that manufacturing process was going in the premises.

**Answer 8(vii)**

The employer is liable to pay compensation.

In the given problem, the worker lost his mental balance as a result of an injury by accident and committed suicide. Suicide is the effect of injury sustained by him and is not while working for personal benefit or acting outside the scope of his employment. Consequently the employer will be held liable. To succeed in claim, it must be proved that the injury arose out of and in the course of employment because compensation is permitted only for those injuries which are sustained in the course of employment and arise out of employment. If that is not proved, no compensation can be claimed by the workman's dependents.

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## SECURITIES LAWS AND COMPLIANCES

Time allowed : 3 hours

Maximum marks : 100

### PART A

(Answer Question No. 1 which is **COMPULSORY**  
and any three of the rest from this part)

#### Question 1

- (a) State, with reasons in brief, whether the following statements are true or false :
- (i) 'Derivatives' are contracts which do not derive their value from any assets.
  - (ii) Trustees are required to disclose the basis of calculation of repurchase price and NAV of various schemes of mutual fund.
  - (iii) Participatory notes are derivative instruments.
  - (iv) 'Underwriter' means a person who engages in the business of selling of an issue of securities of a body corporate.
  - (v) The collective investment management company is not permitted to launch any scheme for the purpose of investing in securities. (2 marks each)
- (b) Choose the most appropriate answer from the given options in respect of the following :
- (i) A company cannot buy-back the securities from —
    - (a) Free reserves
    - (b) Securities premium account
    - (c) Borrowed money
    - (d) Proceeds of fresh issue.
  - (ii) Duration of future contract on NSE is —
    - (a) One month
    - (b) Two months
    - (c) Three months
    - (d) Six months.
  - (iii) Certificate of deposits are issued in the form of —
    - (a) Bill of exchange
    - (b) Usance bill of exchange
    - (c) Usance promissory notes
    - (d) Term deposit.
  - (iv) Venture capital funds are regulated by —
    - (a) RBI
    - (b) SEBI
    - (c) Stock exchange
    - (d) Ministry of Corporate Affairs.

(v) *FCCBs are unsecured and carry interest at —*

(a) *Variable rate*

(b) *Fixed rate*

(c) *Floating rate*

(d) *Not determined.*

*(1 mark each)*

**Answer 1(a)(i)**

**False**

Derivatives are contracts which derive values from the value of one or more of other assets, called underlying assets.

**Answer 1(a)(ii)**

**True**

The AMC shall disclose the basis of calculating the repurchase price and NAV of the various schemes of the fund in the scheme particulars and disclose the same to the investors at such intervals as may be specified by the trustees and SEBI.

**Answer 1(a)(iii)**

**True**

Participatory notes are derivative instruments which are issued by FII to foreign investors.

**Answer 1(a)(iv)**

**False**

'Underwriter' means a person who engages in the business of underwriting of an issue of securities of a body corporate.

**Answer 1(a)(v)**

**True**

The Collective Investment Management Company should not launch any scheme for the purpose of investing in securities.

**Answer 1(b)(i)**

(c) Borrowed money

**Answer 1(b)(ii)**

(c) Three months

**Answer 1(b)(iii)**

(c) Usance promissory notes.

**Answer 1(b)(iv)**

(b) SEBI

**Answer 1(b)(v)**

- (b) Fixed rate

**Question 2**

- (a) Distinguish between any two of the following :

(i) 'French auction' and 'Dutch auction'.

(ii) 'Cut off yield' and 'cut off price'.

(iii) 'Initial margin' and 'maintenance margin'. (4 marks each)

- (b) "Certain securities are not available to a company for buy-back." Explain.

(4 marks)

- (c) Expand the following :

(i) FCCB

(ii) CIS

(iii) SPN. (1 mark each)

**Answer 2(a)(i)****'French auction' and 'Dutch auction'**

There are two types of auction for treasury bills. In French Auction, also known as Multiple Price Based Auction, all bids equal to or above the cut-off price are accepted. However, the bidder has to obtain the treasury bills at the price quoted by him. This method is followed in the case of 364 days treasury bills and is valid only for competitive bidders.

In Dutch auction, also known as Uniform Price Based Auction, all the bids equal to or above the cut-off price are accepted at the cut-off level. However, unlike the Multiple Price based method, the bidder obtains the treasury bills at the cut-off price and not the price quoted by him. This method is applicable in the case of 91 day treasury bills only. The system of Dutch auction has been done away with by the RBI w.e.f. 08.12.2002 for the 91 day treasury T.Bill.

**Answer 2(a)(ii)****'Cut off yield' and 'Cut off Price'**

Cut off yield is the rate at which bids are accepted. Bids at yields higher than the cut-off yield are rejected and those lower than the cut-off are accepted. The cut-off yield is set as the coupon rate for the security. Bidders who have bid at lower than the cut-off yield pay a premium on the security, since the auction is a multiple price auction.

Cut off price is the minimum price accepted for the security. Bids at prices lower than the cut-off are rejected and at higher than the cut-off are accepted. Coupon rate for the security remains unchanged. Bidders who have bid at higher than the cut-off price pay a premium on the security, thereby getting a lower yield. Price based auctions lead to finer price discovery than yield based auctions.

**Answer 2(a)(iii)****‘Initial Margin’ and ‘Maintenance Margin’**

“Initial margin” in this context means the minimum amount, calculated as a percentage of the transaction value, to be placed by the client, with the broker, before the actual purchase. The broker may advance the balance amount to meet full settlement obligations.

“Maintenance margin” means the minimum amount, calculated as a percentage of market value of the securities, calculated with respect to last trading day’s closing price, to be maintained by client with the broker.

**Answer 2(b)**

Regulation 19(5) of SEBI (Buy Back of Securities) Regulations, 1998 provides that the following Securities are not available to a company for buy-back:

- (i) Securities in lock-in period: Securities in lock-in period as per SEBI (DIP) guidelines are not available for buyback until the lock-in period expires.
- (ii) Non-transferable Securities: Securities which are under lien or are pledged or restricted by Court.
- (iii) Disputed Securities kept in abeyance: Securities which are under dispute and have kept in abeyance under section 206A or in respect of which transfer or transmission has not been effected.

**Answer 2(c)(i)**

FCCB - Foreign Currency Convertible Bonds

**Answer 2(c)(ii)**

CIS - Collective Investment Scheme

**Answer 2(c)(iii)**

SPN - Secured Premium Note

**Question 3**

(a) Write short notes on any four of the following :

- (i) Dual option warrants
- (ii) Securities Appellate Tribunal
- (iii) Escrow account
- (iv) Hybrid instrument
- (v) Exchange traded fund. (2 marks each)

(b) Explain the procedure for grant of registration certificate to venture capital fund by SEBI and effect of refusal to grant the certificate. (4 marks)

(c) Explain the term ‘demat’. State the benefits of demat securities. (3 marks)

**Answer 3(a)(i)****Dual Option Warrants**

Dual option warrants are designed to provide the buyer with good potential of capital appreciation and limited downside risk. Dual option warrants may be used to sell equity shares in different markets. For example, equity shares or debentures may be issued with two warrants - one warrant giving right to the purchaser to be allotted one equity share at the end of a certain period and another warrant with a debt or preference share option.

**Answer 3(a)(ii)****Securities Appellate Tribunal**

The Central Government may, by notification establish an appellate tribunal known as Securities Appellate Tribunal (SAT) to exercise the jurisdiction, powers and authority conferred on such tribunal under the SEBI Act, 1992. The Central Government has set up a Tribunal at Mumbai. Any person aggrieved by the order of the SEBI may refer an appeal to a Securities Appellate Tribunal having jurisdiction in the matter. The SAT is not bound by the Code of Civil Procedure, 1908 but is guided by the principle of natural justice and has the powers to regulate its own proceedings.

**Answer 3(a)(iii)****Escrow Account**

Escrow Account means an account in which money is held until a specified duty is performed. Escrow account is opened by the issuing company in case of public issue of securities, buy back of securities, take over etc. A sum prescribed under the Regulations/ Guidelines is transferred to the Escrow Account unless the said formalities regarding the event are over. The Escrow Account may consist of cash deposited with a schedule commercial bank, bank guarantee in favour of merchant banker, deposit of acceptable securities with appropriate margin with the merchant banker.

**Answer 3(a)(iv)****Hybrid instrument**

Hybrid instrument is an instrument which is created by combining the features of equity and debt e.g. Convertible preference shares, Cumulative convertible preference shares, non convertible debentures with equity warrants, partly convertible debentures, partly convertible debentures with Khokha (buy-back arrangement), Optionally convertible debenture, warrants convertible into debentures or shares, secured premium notes with warrants etc.

**Answer 3(a)(v)****Exchange Traded Fund**

Exchange Traded Fund (ETF) represent a basket of securities that are traded on an exchange. It is similar to index mutual fund but is traded more like a stock. It is a rapidly growing class of financial product and is typically organized as unit trust. ETF can be bought and sold throughout the trading day, allowing for intraday trading - which is rare



with mutual funds. Unlike mutual funds, ETF do not trade necessarily at the net asset value of its underlying holding, meaning an ETF could potentially trade above or below the value of the underlying portfolio.

### **Answer 3(b)**

#### **Procedure for grant of certificate to Venture Capital Fund**

SEBI after getting satisfied that the applicant is eligible for the grant of certificate should send intimation to the applicant and after the receipt of intimation, the applicant should pay the registration fee as specified. SEBI on receipt of the registration fee grants a certificate of registration. The venture capital fund should abide by the provisions of the Act. It should not carry on any other activity other than that of a venture capital fund and should forthwith inform SEBI in writing. Otherwise the decision of SEBI to reject the application should be communicated to the applicant within 30 days.

#### **Effect of refusal to grant certificate**

Any applicant whose application has been rejected cannot carry on any activity as a venture capital fund. Thus any company or trust or a body corporate whose application for grant of certificate has been rejected by SEBI should on and from the date of the receipt of the communication cease to carry on any activity as a venture capital fund.

### **Answer 3(c)**

#### **Demat**

'Demat' refers to dematerialisation which is a process by which the physical share certificates of an investor are taken back by the Company and an equivalent number of securities are credited to the investors account in electronic form at the request of the investor.

#### **Benefits of Demat Securities**

- Elimination of bad deliveries
- Elimination of all risks associated with physical certificates
- Immediate transfer and registration of securities
- Faster disbursement of non cash corporate benefits like rights, bonus, etc.
- Reduction in handling of huge volumes of paper

#### **Question 4**

- (a) *What action lies against SEBI registered intermediaries in case of default/violation under the SEBI Act, 1992 ?* (4 marks)
- (b) *Briefly discuss the guidelines for issue of commercial paper.* (4 marks)
- (c) *"Corporate Governance is the application of best management practices."*  
*Comment.* (4 marks)
- (d) *Explain the following credit rating symbols —*
- (i) ER1A
  - (ii) ER1C
  - (iii) M1. (1 mark each)

**Answer 4(a)**

Chapter VIA of SEBI Act, 1992, contains Section 15A to 15J which deals with penalties which can be imposed under the Act for various failures, defaults, non-disclosure and other offences.

Section 15B and 15C lays specific action in case of default /violation by intermediaries under the SEBI Act, 1992.

SEBI (Intermediaries) Regulations, 2008 provide for the imposition of any of the following penalties as the case may be,

## (i) Minor Penalties-

- (a) Censure
- (b) Prohibiting the intermediary to take up any new assignment or mandate or launch a new scheme for a period up to six months.
- (c) Debarring a partner or a whole time director of the intermediary from carrying out the activities as intermediary in the intermediary firm or company and other capital market related institutions for a period up to six months.
- (d) Suspension of certificates of registration for a period up to three months.
- (e) Debarring a branch or an officer of the intermediary from carrying out the activities for a period upto six months.

## (ii) Major Penalties-

- (a) Cancellation of certificates of registration.
- (b) Suspension of certificate of registration for a period exceeding three months,
- (c) Taking of action under sub-clause b, c or e of Clause (i) for a period exceeding six months.

**Answer 4(b)**

The Guidelines provide eligibility criteria as to net worth, working capital limit for issue of commercial paper. The requirements are as under:

1. *Rating Requirement*- All eligible participants shall obtain the credit rating for issuance of Commercial Paper from the Credit Rating Agencies registered with SEBI.
2. *Maturity*- CP can be issued for maturities between a minimum period of 7 days and a maximum up to one year from the date of the issue.
3. *Denominations*- CP can be issued in denominations of Rs.5 lakh or multiples thereof. Amount invested by a single investor should not be less than Rs.5 lakh (face value).
4. *Limits and the Amount of Issue of CP*- CP can be issued as a “stand alone” product.
5. *Issuing and Paying Agent (IPA)* - Every issuer must appoint an IPA for issuance of CP. Only a scheduled bank can act as an IPA.

6. *Mode of Issuance* - CP can be issued either in the form of a promissory note or in a dematerialized form.
7. *Preference for Dematerialization* - Banks, FIs and PDs are required to make fresh investments and hold CP only in dematerialized form.

**Answer 4(c)**

The ICSI has defined 'Corporate Governance' to mean that it is the application of best management practices, compliance of law in the letter and spirit and adherence to ethical standards for effective management and distribution of wealth and discharge of social responsibility for sustainable development of all shareholders.

Adoption of best corporate governance practices distinguishes a company from ordinary companies, which are content merely in complying with prescribed legal requirements. The companies adopting "best corporate governance practices" stand out from others. The adoption of such best practices is purely voluntary and depends on the financial and other capabilities of the company apart from the commitment of the company to values and ethical business.

**Answer 4(d)(i)**

**ER1A** — Excellent Earnings Prospects; Low Risk (ICRA Equity Grade).

**Answer 4(d)(ii)**

**ER1C** — Excellent Earnings prospects; High Risk(ICRA Equity Grade).

**Answer 4(d)(iii)**

**M1** – Indicates very low sensitivity to changing interest rates and other market conditions (ICRA Debt Fund Rating).

**Question 5**

(a) *Explain the following terms related to capital market :*

- (i) *Incubators*
- (ii) *Angel investors*
- (iii) *Private equity players.*

(2 marks each)

(b) *Ajay purchases 8.4% Government of India Bond, 2018 of face value of Rs.20 lakh @ Rs.102.50 for every unit of security having face value of Rs.100. The settlement is due on 13th October, 2009. What is the amount to be paid by Ajay? (Assuming that interest is payable on 13th May and 13th November every year.)*

(5 marks)

(c) *Discuss the regulatory framework governing primary market intermediaries.*

(4 marks)

**Answer 5(a)(i)****Incubators**

An incubator is a hardcore technocrat who works with an entrepreneur to develop a business idea, and prepares a Company for subsequent rounds of growth & funding. E-Ventures, Infinity are examples of incubators in India.

**Answer 5(a)(ii)****Angel Investors**

An angel is an experienced industry-bred individual with high net worth. Typically, an angel investor would invest only in his chosen field of technology, take active participation in day-to-day running of the Company, invest small sums and does not insist on detailed business plans sanction.

**Answer 5(a)(iii)****Private Equity Players**

They are established investment bankers. They typically invest into proven/ established businesses. They have “financial partners” approach and invest between USD 5-100 million.

**Answer 5(b)**

Coupon rate — 8.4%

Year of maturity — 2018

Face value of Rs. 20 lacs @ Rs.102.50

Therefore, the principal amount payable is Rs.20 lacs x 102.50

= Rs. 20,50,000

Interest for the period from 13-5-08 to 13-10-08

No of days	May	18
	June	30
	July	30
	Aug.	30
	Sep.	30
	Oct.	12
		<u>150</u>

Interest payable =  $\frac{20,00,000 \times 8.40 \times 150}{360 \times 100} = \text{Rs. } 70,000$

Total amount to payable by Mr. X = Rs. 20,50,000 + Rs. 70,000  
= Rs. 21,20,000

*Note : For Government dated securities, the day count is taken as 360 days for a year and 30 days for every completed month.*

**Answer 5(c)**

Primary market intermediary is the intermediary connected to the issue of securities by the issuer company in the primary market. Various market intermediaries are involved in the primary markets are Merchant Bankers/Lead managers, Registrars and Share Transfer Agents, Underwriters and Bankers to Issue.

These market intermediaries operate under regulatory framework of SEBI Act, 1992, Securities Contracts (Regulation) Act, 1956, Securities Contracts (Rules), 1957. As per Section 11 of SEBI Act, 1992 it is the duty of SEBI to register and regulate the intermediaries in primary and secondary market. SEBI has also issued regulations in respect of each intermediary to ensure proper services to be rendered by them to the investors and the capital market e.g. SEBI (Underwrites) Regulations, SEBI (Banker to an Issue) Regulations, SEBI (Prohibition of Insider Trading) Regulations, 1992, etc. SEBI has also issued SEBI (Intermediaries) Regulations 2008, to put in place a comprehensive framework which will apply to the intermediaries. The new regulation provides for all intermediaries to register and regulate the permanent registration, multiple registration form, fit and proper person criteria, suspension and cancellation of certificate of registration.

### **PART B**

*(Answer ANY TWO questions from this part.)*

#### **Question 6**

- (a) *What is Indian Depository Receipt (IDR) ? What are eligibility criteria for issue of IDRs ?* (5 marks)
- (b) *What is 'price stabilization fund' ?* (5 marks)
- (c) *Write a note on 'due diligence' in the process of public issue of securities.* (5 marks)
- (d) *State the powers and functions of the 'Ombudsman' under the SEBI (Ombudsman) Regulations, 2003.* (5 marks)

#### **Answer 6(a)**

##### **Indian Depository Receipts**

"Indian Depository Receipt" (IDR) means any instrument in the form of a depository receipt created by Domestic Depository in India against the underlying equity shares of issuing company.

##### **Eligibility for issue of IDRs**

Companies (Issue of Indian Depository Receipts) Rules, 2004 provides that an issuing company shall not issue IDRs unless it satisfies the following conditions, namely-

- (a) Its pre-issue paid-up capital and free reserves are at least US \$50 million and it has a minimum average market capitalization (during the last 3 years) in its parent country of at least US \$ 100 million.
- (b) It has a continuous trading record or history on a stock exchange in its parent country for at least three immediately preceding years.
- (c) It has a track record of distributable profits in terms of Section 205 of the Companies Act, 1956, for at least three out of immediately preceding five years.
- (d) It fulfills such eligibility criteria as may be laid down by SEBI from time to time in this behalf.
- (e) Its Pre issue debt equity ratio is not more than 2:1.

SEBI (DIP) Guidelines, 2000 provides eligibility criteria for issue of IDR- the issuer company should be listed in its home country; has not been prohibited to issue securities by any Regulatory Body and has a good track record with respect to compliance with securities market regulations.

**Answer 6(b)**

The fund created to cause stabilization of the share price of an entity specially after the public issue of securities is known as price stabilization fund. The aim of the fund is to project the share price from falling below the issue price. For the purpose of operating a price stabilization mechanism post listing the issuer company appoints a stabilization agents (SA). The prime responsibility of SA shall be to stabilize post listing price of shares. To this end, SA shall determine the timing of buying the shares, the quantity to be bought, the price at which the shares are to be bought etc. stabilization mechanism shall be available for the period disclosed by the company in the prospectus which shall not exceed 30 days from the date when trading permission was given by the exchanges.

**Answer 6(c)**

**Due Diligence**

Due Diligence includes all the activities that are associated with evaluating a proposal. It includes carrying out reference checks on the proposal related aspects. In relation to public issue of securities, due diligence is carried out by a merchant banker. The Lead Merchant Banker is responsible for verification of the contents of a prospectus or the letter of offer in respect of an issue of securities and reasonableness of the views expressed therein and to submit to SEBI at least 2 weeks prior to the opening of issue for subscription, a due diligence certificate in the prescribed form.

In process of due diligence, the Merchant Banker examines various documents including those relating to litigation like commercial disputes, patent disputes, disputes with collaborators etc. and also discuss with the company its directors and other officers and other agencies on matters including objects of the issue, projected profitability, price justification etc. before giving the Due Diligence Certificate.

**Answer 6(d)**

The Ombudsman has the following powers and functions:

- (a) to receive complaints specified under SEBI (Ombudsman) Regulation against any intermediary or a listed company or both;
- (b) to consider such complaints and facilitate resolution thereof by amicable settlement;
- (c) to approve a friendly or amicable settlement of the dispute between the parties;
- (d) to adjudicate such complaints in the event of failure of settlement thereof by friendly or amicable settlement.

The Ombudsman is required to draw up an annual budget for his office in consultation with the Board and shall incur expenditure within and in accordance with the provisions

of the approved budget and submit an annual report to the SEBI within three months of the close of each financial year containing general review of activities of his office. The ombudsman is also under obligation to furnish from time to time such information to SEBI as may be required by the SEBI.

**Question 7**

- (a) *What do you understand by 'offering circular' for Euro-issue ? Mention any five aspects which should be covered in the offering circular. (5 marks)*
- (b) *What are the disclosures in the Directors' Report as per the SEBI (Employee Stock Option Scheme and Employee Stock Purchase Scheme) Guidelines, 1999 ? (5 marks)*
- (c) *Explain the procedure of bidding in book building issue. (5 marks)*
- (d) *Discuss the approvals required from various authorities in issuance of GDRs and FCCBs. (5 marks)*

**Answer 7(a)**

Offering Circular is a document issued by the issuer company through which the prospective investors can access vital information regarding the company in order to form their investment strategies. It is to be prepared very carefully giving true and complete information regarding the financial strength of the company, its past performance, past and envisaged research and business promotion activities, track record of promoters and the company, ability to trade the securities on Euro capital market.

The Offering Circular for Euro-issue offering should typically cover the following contents:

- (i) Background of the company and its promoters including date of incorporation and objects, past performance, production, sales and distribution network, future plans, etc.
- (ii) Capital structure of the company- existing, proposed and consolidated.
- (iii) Deployment of issue proceeds.
- (iv) Financial data indicating track record of consistent profitability of the company.
- (v) Group investments and their performance including subsidiaries, joint venture in India and abroad.
- (vi) Investment considerations.
- (vii) Description of shares.
- (viii) Terms and conditions of global depository receipt and any other instrument issued along with it.
- (ix) Economic and regulatory policies of the Government of India.
- (x) Details of Indian securities market indicating stock exchange, listing requirements, foreign investments in Indian securities,
- (xi) Market price of securities.
- (xii) Dividend and capitalization.

- (xiii) Securities regulations and exchange control.
- (xiv) Tax aspects indicating analysis of tax consequences under Indian law of acquisition, membership and sale of shares, treatment of capital gains tax, etc.
- (xv) Status of approvals required to be obtained from Government of India.
- (xvi) Summary of significant differences in Indian GAAP, UK GAAP and US GAAP and expert's opinion.
- (xvii) Report of statutory auditor.
- (xviii) Subscription and sale.
- (xix) Transfer restrictions in respect of instruments.
- (xx) Legal matters etc.
- (xxi) Other general information not forming part of any of the above

*NOTE : Students may mention any five points mentioned above.*

**Answer 7(b)**

Directors' report shall contain the following disclosures about ESOP Scheme:

- (i) The total number of shares covered by the ESOP as approved by the shareholders;
- (ii) The pricing formula;
- (iii) Options granted, options vested, options exercised, options forfeited, extinguishment or modification of options, money realized by exercise of options, total number of options in force, employee-wise details of options granted to senior managerial personnel and to any other employee who receive a grant in any one year of options amounting to 5% or more of options granted during that year;
- (iv) Fully diluted earning per share (EPS) computed in accordance with International Accounting Standards.

The Director's Report related to ESOP should contain the following disclosures:

- (a) the details of the number of shares issued in the scheme;
- (b) the price at which such shares are issued;
- (c) employee-wise details of the shares issued to: senior managerial personnel; any other employee who is issued shares in any one year amounting to 5% or more shares issued during that year; identified employees who were issued shares during any one year equal to or exceeding 1% of the issued capital of the company at the time of issuance.
- (d) diluted Earning Per Share (EPS) pursuant to issuance of shares under the scheme; and
- (e) consideration received against the issuance of shares.

**Answer 7(c)**

**Bidding Procedure**

- (i) Individual as well as qualified institutional buyers shall place their bids only through the 'brokers' who shall have the right to vet the bids. The applicant shall



- enclose the proof of DP ID and Client ID along with the application, while making bid.
- (ii) During the period the issue is open to the public for bidding, the applicants may approach the brokers of the stock exchange/s through which the securities are offered under on-line system, to place an order for bidding to the securities.
  - (iii) Every broker shall accept orders from all clients/investors who place orders through him. The investors shall have the right to revise their bids provided that Qualified Institutional Buyers shall not be allowed to withdraw their bids after the closure of the bidding.
  - (iv) There shall be a standard bidding form to ensure uniformity in bidding and accuracy.
  - (v) At the end of each day of the bidding period the demand shall be shown graphically on the terminals for information of the syndicate members as well as the investors. The identities of the Qualified Institutional Buyers making the bidding, would however not be made public.

**Answer 7(d)**

The following approvals are required for issue of Global Depository Receipts (GDRs) and Foreign Currency Convertible Bonds (FCCBs)

- (1) A meeting of Board of Directors is required to be held for approving the proposal to raise money from Euro Capital market, through board resolution indicating therein specific purposes for which funds are required, quantum of the issue, country in which issue is to be launched, time of the issue etc.
- (2) A special resolution under Section 81(1A) of the Companies Act, 1956 is required to be passed at a duly convened general meeting of the shareholders of the company.
- (3) Approval from Ministry of Finance is required for FCCB issues exceeding stipulated limit
- (4) The issuer company has to obtain approvals from Reserve Bank of India under circumstances specified under the guidelines issued by the concerned authorities from time to time.
- (5) The issuing company has to make a request to the domestic stock exchange for in-principle consent for listing of underlying shares which shall be lying in the custody of domestic custodian.
- (6) The company is required to obtain in principle consent of Financial Institutions on the broad terms of the proposed issue.

**Question 8**

- (a) *“SEBI expects the investors to make investments with their eyes and ears open.” Comment.* (5 marks)
- (b) *Discuss the end use of external commercial borrowings under approval route.* (5 marks)

(c) *Discuss the various formalities to be complied with for the issue of bonus shares under the SEBI (Disclosure and Investor Protection) Guidelines, 2000.*

(10 marks)

**Answer 8(a)**

Protection of the investor has been the main concern of SEBI. SEBI has issued various Guidelines, Circulars, Instructions relating to issue of capital. Disclosure of full and fair details of all aspects of securities issued has been made the corner stone of Capital Mobilization by Corporates. The various Guidelines emphasise the need to give full disclosure of facts in the issue documents, advertisements, prospectus etc. SEBI has issued a number of Regulations on different intermediaries, which are binding on them. However, SEBI expects the investors to make investments with their eyes and ears open and expects investors to go through the disclosures contained in the various documents issued by the company and make an informed decision before investing. For this purpose investors have to educate themselves on the fundamental aspects of choosing the securities, understanding the past record and future prospects of the companies plans. SEBI has also issued Investor Education Guide, which contains briefly the Risk of Corporate Investments, Investors Rights and Responsibilities, basics of Trading in Securities, Transfer and Transmission of Securities, Depository and Dematerialisation of Share Certificates and Grievance redressal mechanism available.

**Answer 8(b)**

**Utilization of ECB Proceeds**

ECB proceeds can be utilized for overseas direct investment in Joint Ventures (JV)/ Wholly Owned Subsidiaries (WOS) subject to the existing guidelines on Indian Direct Investment in JV/WOS abroad.

Utilisation of ECB proceeds is permitted in the first stage acquisition of shares in the disinvestments process and also in the mandatory second stage offer to the public under the Government's disinvestments programme of PSU shares.

However, utilization of ECB proceeds is not permitted for on-lending or investment in capital market by corporates.

Utilisation of ECB proceeds is also not permitted in real estate. The term 'real estate' excludes development of integrated township.

End-uses of ECB for working capital, general corporate purpose and repayment of existing Rupee loans are also not permitted.

**Answer 8(c)**

**The Requirements to be complied with while making a Bonus Issue are given hereunder:**

1. *Rights of FCD/PCD holders*

The proposed bonus issue should not dilute the value or rights of the fully or partly convertible debentures.

2. *Out of Free Reserves*

The bonus issue is to be made out of free reserves built out of the genuine profits or securities premium collected in cash only.

3. *Revaluation Reserves*

The reserves created by revaluation of fixed assets should not be capitalised.

4. *Bonus Issue not to be in lieu of Dividend*

Bonus issue should not be made in lieu of dividend.

5. *Fully Paid Shares*

If there are any partly paid-up shares, these shares should be made fully paid-up before the bonus issue is made.

6. *No Default in respect of Fixed Deposits/Debentures*

The company should not have defaulted in the payment of any interest or principal in respect of its fixed deposits and interest on debentures or on redemption of debentures.

7. *Statutory Dues of the Employees*

The company should not have defaulted in the payment of its statutory dues to the employees such as contribution to provident fund, gratuity, bonus, minimum wages, workmen's compensation, retrenchment compensation, payments to contract labour, etc.

8. *Implementation of Proposal within Six Months*

The bonus issue should be made within a period of six months from the date of approval of the Board of directors. The company cannot reverse the decision once it has been taken by the Board of directors.

9. *Provision in Articles of Association*

The Articles of Association of the Company should provide for capitalisation of reserves and if not a General Body Meeting of the company is to be held and a special resolution making provisions in the Articles of Association for capitalisation should be passed.

10. *Authorised Capital*

If consequent upon the issue of bonus shares, the subscribed and paid-up capital of the company exceed the authorised share capital, a General Meeting of the company should be held to pass necessary resolution for increasing the authorised capital.

11. *Compliance Certificate*

A certificate duly signed by the issuer company and counter signed by statutory auditor or by Company Secretary in practice to the effect that the provisions for issue of bonus shares under the SEBI (DIP) Guidelines, 2000 have been complied with shall be forwarded to the SEBI.

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