Paper- 11: CAPITAL MARKET ANALYSIS & CORPORATE LAWS

Time Allowed: 3 Hours **Full Marks:** 100

The figures in the margin on the right side indicate full marks.
Please: (1) Answer all bits of a question at one place.
(2) Answers to each question should start from a new page.
Example: Q. No. 2/3/any should start from a new page.
(3) Working notes should form part of your answer

SECTION - I (60 Marks)
(Capital Market Analysis)

Answer Question No. 1 (compulsory) and answer any two from the rest in this Section.

Question 1.

(a) In each of the cases given below indicate the correct answer and give workings/ reasons briefly in support of your answer. [2×6]

(i) Mr. Ray has purchased 100 shares of ₹ 10.00 each, of Kinetic Ltd. in 2012 at ₹ 78.00 per share. The company has declared a dividend @ 40% for the year 2013-14. The market price of share as at 1.4.2013 was ₹ 104 and on 31.03.2014 was ₹ 128.00. Calculate the annual return on the investment for the year 2013-14.

(ii) The unit price of RSS Scheme of a mutual fund is ₹ 10. The Public Offer Price (POP) of the unit is ₹ 10.204 and the redemption price is ₹ 9.80. Calculate the front-end load.

(iii) A 3 month future contract on Nifty is available at a time when Nifty is quoting 9,000 points. Continuously compounded risk free rate is 10%. Continuously compounded yield on the Nifty stock is 2% p.a. how much will you pay for Nifty futures. If Nifty forward trades at 9,125, would you prefer to purchase Nifty forward or Nifty futures for your portfolio?

(iv) T.S. Kumar holds a two-stock portfolio. Stock ABC has a standard deviation of returns of 0.6 and stock XYZ has a standard deviation of 0.4. The correlation coefficient of the two stocks returns is 0.25. Kumar holds equal amounts of each stock. Compute the portfolio standard deviation for the two-stock portfolio.

(v) An investor has ₹ 5,00,000 to invest. What will be his expected risk premium in investing in equity versus risk-free securities in the following conditions:

Investment	Probability	Expected return
Equity	0.6	₹ 2,00,000
	0.4	(-) ₹ 1,50,000
Risk-free security	1.0	₹ 25,000

(vi) Maruti has a beta of 0.865. If the expected market return is 17.50 and the risk free rate of return is 8.50%, what is the appropriate required return of Maruti (using the CAPM)?

Answer:

(i) Calculation of annual rate of return on investment for the year 2013-14:

$$R = \frac{D_1 + (P_1 - P_0)}{P_0}$$

$$= \frac{₹\ [4 + (128 - 104)]}{₹\ 104} = 0.2692$$

Or, 26.92%.

(ii) Calculation of Front-end load

$$\text{Public Offer Price} = \frac{\text{Net asset value}}{1 - \text{front} - \text{end load}}$$

Where, POP is ₹ 10.204; Net Asset Value (NAV) is ₹ 10.

$$10.204 = \frac{10}{(1 - \text{front} - \text{end load})}$$

10.204 (1– front-end load) =10,

10.204 – 10.204 front-end load =10,

10.204 front-end load = 10.204 – 10,

$$\text{Front} - \text{end load} = \frac{0.204}{10.204} = 0.01999,$$

So, Front-end load =2%.

(iii) Current future price of Nifty = S (1 + cost of carry – dividend yield)

= 9,000 × $e^{(0.10 - 0.02)\times 0.25}$ = ₹ 9,181.80

Since, actual forward price is ₹ 9,125 which is less than Current Future Price of Nifty, hence, Nifty forward may be bought.

(iv) $$\sigma_p = \sqrt{(0.5)^2 \times (0.6)^2 + 2 \times 0.5 \times 0.5 \times 0.6 \times 0.4 \times 0.25 + \left(0.5\right)^2 \times (0.4)^2}$$

$$= \sqrt{0.09 + 0.03 + 0.04}$$

$$= \sqrt{0.16} = 0.4$$

(v) Expected premium = (0.6 x ₹ 2,00,000) + [0.4 x (-) ₹ 1,50,000] – ₹ 25,000

= ₹ 1,20,000 – ₹ 60,000 – ₹ 25,000 = ₹ 35,000

(vi) Required rate of return:

= 8.50% + (17.5% - 8.5%) x 0.865

= 8.50% + 9.0% x 0.865

= 8.50% + 7.785%

= 16.285%

(b) Choose the most appropriate one from the stated options and write it down (only indicate A or B or C or D as you consider correct). **[1 x 5 = 5]**

(i) The fixed price at which the option holder can buy or sell the underlying asset is called the —

A. **Strike price;**
B. **Spot price;**
C. **Market price;**
D. **Future price.**

(ii) Father of modern portfolio theory —
A. **John Litner;**
B. **Harry Markowitz;**
C. **Jensen;**
D. **William F. Sharpe.**

(iii) Arbitrage pricing theory model helps to —
A. **Reduce risk;**
B. **Eliminate arbitrage;**
C. **Identify the equilibrium asset price;**
D. **None of the above.**

(iv) Residual analysis is a test of —
A. **Weak form of market efficiency;**
B. **Semi-strong form of market efficiency;**
C. **Strong form of market efficiency;**
D. **Super-strong form of market efficiency.**

(v) As the business cycle enters the initial phase of economic recovery the stock prices generally:
A. **Decline;**
B. **Maintain the same trend as before;**
C. **Rise;**
D. **Rise to an extent and then take a downturn.**

Answer:

(i) A.
(ii) B.
(iii) C.
(iv) B.
(v) A.

(c) Fill in the blanks in the following sentences by using appropriate word(s) / phrase(s) / number(s): [1x3=3]

(i) ________________ is a capital issuance process which results towards a price discovery and also to assess demand analysis of the security.

(ii) The functions of ________________ cover a wide range of activities such as management of customer services, portfolio management, credit syndication, acceptance credit, counselling, insurance etc.

(iii) A ________________________ is a scheme of investing money with other people to participate in a wider range of investments than may be feasible for an individual investor, and to share the costs of doing so.

Answer:

(i) Book Building
(ii) merchant banking
(iii) collective investment scheme

Question 2.

(a) An investor buys a put option having a strike price of ₹ 1,000 by paying premium of ₹ 90. He also sells a put option having a strike price of ₹ 900 and receives premium of ₹ 50. You are required to —

(i) Compute the cost of strategy.
(ii) Compute the breakeven point.
(iii) Compute the profit/ loss from the strategy, if the price on maturity is ₹ 800, ₹ 880, ₹ 950, ₹ 980, ₹ 1,000, and ₹ 1,070. [1+1+3]

Answer:

(i) Cost of strategy = ₹ 90 – ₹ 50 = ₹ 40.
(ii) Break Even Point = Strike price of bought-out option + premium charged – premium paid = ₹ 1,000 + ₹ 50 – ₹ 90 = ₹ 960.
(iii) Computation of profit/ loss from the strategy:

Price on maturity (₹)	Profit/ (loss) (₹)	
800	1,000 – 900 - 40	= 60
880	1,000 – 900 - 40	= 60
950	1,000 – 950 - 40	= 10
980	1,000 – 980 - 40	= (20)
1,000		(40)
1,070		(40)

(b) Explain Bought Out Deal. State the advantages of it (any four). [3+4]

Answer:

Bought out Deal (BOD):

Bought out Deal (BOD) is a process of investment by a sponsor or a syndicate of investors/ sponsors directly in a company. Such direct investment is being made with an understanding between the company and the sponsor to go for public offering in a mutually agreed time.

Bought out deal, as the name suggests is a type of wholesale offer of equities by a company. A company allots shares in full or in lots to a sponsors at a price negotiated between the company and the sponsor(s). After a particular period of agreed upon between the sponsorer and the company the shares are issued to the public by the sponsorer with a premium.

The holding cost of such shares by the sponsor may either be reimbursed by the company or the sponsor may absorb the profit in part or full as per the agreement, arising out of the public offering at a premium. After the public offering the shares are listed in one or more stock exchanges.

Advantages of Bought out Deal:
It is not only advantageous to the company going for it but also to the sponsors and common investors:

1. The company has the advantage of using the fund immediately without waiting as in the case of direct public issue. In case of BOD the company instantly gets funds and is able to focus its attention on project implementation without worrying for source of investment. Bought out deals are ideally suited in circumstances when money needs to be arranged fast without which the project may suffer. Lowering or eliminating issue cost from the preliminary expenses is another advantage to the company.

2. The time taken to raise money in the capital market by a company takes much and this time is very high for a company in an infancy stage. The waste of time in the initial stage can be avoided by going for BOD.

3. In case of a new and untried product it is easier to convince an investment banker for an investment in the company rather than the general public. Hence BOD is an innovative method of financing for such companies.

4. When the market sentiment is low and the secondary market is undergoing a bear phase, a company may not like to come to the market with a public issue. In such case BOD is a superior process to get fund for the company.

5. The merchant bankers also gain handsomely from a BOD. The gains can be tremendous provided the sponsors select proper issues and price it attractively to the investors.

6. The investors also gain from the BOD in a way that they get good issues where some merchant banker has already invested in it. The common investors do not have enough scope and information for proper evaluation of a company. The merchant bankers are professionals and can make proper appraisal of a company.

(c) Expected returns on two stocks for particular market returns are given in the following table:

Market Return	Aggressive	Defensive
7%	4%	9%
25%	40%	18%

You are required to calculate:
(i) The Betas of the two stocks.
(ii) Expected return of each stock, if the market return is equally likely to be 7% or 25%.
(iii) The Security Market Line (SML), if the risk free rate is 6.5% and market return is equally likely to be 7% or 25%.
(iv) The Alphas of the two stocks. [2+2+2+2]

Answer:

(i) Calculation of Betas of two stocks:

$$\text{Aggressive stock} = \frac{40\% - 4\%}{25\% - 7\%} = \frac{36\%}{18\%} = 2$$

$$\text{Defensive stock} = \frac{18\% - 9\%}{25\% - 7\%} = \frac{9\%}{18\%} = 0.5$$

(ii) Calculation of Expected Return of Each Stock:
Aggressive stock = (4% × 0.5) + (40% × 0.5) = 22%
Defensive stock = (9% × 0.5) + (18% × 0.5) = 13.5%

(iii) Calculation of Security Market Line (SML):
Expected Return of Market Portfolio = (7% × 0.5) + (25% × 0.5) = 16%
Market Risk Premium = 16% - 6.5% = 9.5%
SML = 6.5% + β_i 9.5%.

(iv) Calculation of Alphas of the two stocks:
Alpha for Aggressive stock = 0.22 - [0.065 + (2 × 0.095)] = 0.22 - 0.255 = - 3.5%
Alpha for Defensive stock = 0.135 - [0.065 + (0.5 × 0.095)] = 0.135 - 0.1125 = 2.25%

Question 3.

(a) Following is the data regarding six securities:

	A	B	C	D	E	F
Return (%)	**10**	**10**	**15**	**6**	**11**	**10**
Risk (%) (Standard deviation)	**5**	**6**	**13**	**6**	**6**	**7**

(i) Which of three securities will be selected?
(ii) Assuming perfect correlation, analyse whether it is preferable to invest 80% in security A and 20% in security C or to invest 100% in E. [2+2]

Answer:

(i) When we make risk-return analysis of different securities from A to F, we can observe that security A gives a return of 10% at risk level of 5%. Simultaneously securities B and F give the same return of 10% as of security A, but their risk levels are 6% and 7% respectively. Security D is giving only 6% return for the risk rate of 6%. Hence, security A dominates securities B, D and F. Securities C and E offer more return but it carries higher level of risk. Hence securities A, C and E can be selected based on individual preferences.

(ii) In a situation where the perfect positive correlation exists between two securities, their risk and return can be averaged with the proportion. Assuming the perfect correlation exists between the securities A and C, average risk and return of A and C together for proportion 4:1 is calculated as follows:

Risk = [(4 × 0.05) + (1 × 0.13)] ÷ 5 = 6.6%
Return = [(4 × 0.10) + (1 × 0.15)] ÷ 5 = 11%

When we compare risk of 6.6% and return of 11% with security E with 6% risk and 11% return, security E is preferable over the portfolio of securities A and C in proportion of 4:1.

(b) "The contract of insurance is required to fulfill the principles of insurance ......" — describe those principles. [6]

Answer:
There are six principles of insurance namely;
- Insurable Interest;
- Indemnity;
- Subrogation;
- Proximate Cause;
- Good Faith;
- Consideration.

1. Insurable Interest: The Insured must have the insurable interest in the subject matter of insurance i.e., benefit by its safety or prejudiced by its loss.

2. Indemnity: The insured person is placed financially, in the same position as he was before the loss.

3. Subrogation: The legal right of one person, having indemnified the other in a contractual obligation to assume the place of another and avail all rights and remedies of another, whether enforced or not. Example: The Insurer of an importer of electrical goods receives claims in respect of faulty toaster. The insurer pays the claim and takes over the insured's right to claim from the manufacturer.

4. Proximate Cause: The active and efficient cause that sets into motion a train of events, which bring about result/ loss with no other intervening cause. Example: During the war period, a bomb was dropped on a factory, which caused fire to the factory. The proximate cause was enemy action and not fire.

5. Good Faith: the insured is duty bound to disclose all material facts relating to the risk to be covered. Both parties are expected to observe good faith on disclosing the information of the contract.

6. Consideration: Each policy holder is obliged to pay only a rateable portion to the insurer, under each separate policy.

(c) (i) State the characteristics of Forward Contract.
(ii) The following data relates to PQ Ltd.'s share prices:
Current price per share ₹ 180.
Price per share in the futures market-6 months ₹ 197.
It is possible to borrow money in the market for securities transactions at the rate of 12% per annum. Calculate the theoretical minimum price of a 6 month-forward contract.
[2+2]

Answer:
(i) The characteristics of Forward Contract:
- A forward contract is one to one bi-partite contract, to be performed in the future, at the terms decided today.

- Forward contracts offer tremendous flexibility to the parties to design the contract in terms of the price, quantity, quality (in case of commodities), delivery time and place.
- Forward contracts suffer from poor liquidity and default risk.
- Example: forward currency market in India.

(ii) Calculation of Theoretical Minimum Price of a 6-month Forward Contract:
Current share price ₹ 180.

Interest rate prevailing in money market for securities transactions 12%.
Then, Theoretical Minimum Price = ₹ 180 + (₹ 180 × 12/100 × 6/12) = ₹ 190.80.

(d) Mr. Rawal is interested in writing a six-months call option on L&T's share. L&T's share is currently selling for ₹ 120. The volatility (standard deviation) of the share returns is estimated as 67 per cent. Mr. Rawal would like the exercise price to be ₹ 120. The risk-free rate is assumed to be 10 per cent. Calculate the value of the call option? Also calculate the hedge ratio of the call option. **[5+1]**

Answer:
We assume that the share is not a dividend-paying share. Calculations of d_1 and d_2 are as follows:

$$d_1 = \frac{\ln(120/120) + [0.10 + (0.67)^2/2]0.5}{0.67\sqrt{0.5}} = 0.34$$

$d_2 = 0.34 - 0.67\sqrt{0.5} = -0.13$

$N(d_1) = N\ (0.34) = 0.6331$
$N(d_2) = N(-0.13) = 0.4483$

The call option value is calculated as given below:
$C_o = 120\ (0.6331) - 120\ (0.4483)\ e^{-0.1(0.5)}$
$= 75.97 - 120\ (0.4483)(0.9512)$
$= 75.97 - 51.17$
$=$ ₹ 24.80

The hedge ratio of the call option is 0.34, which is the value of $N(d_1)$.

Question 4.

(a) A Mutual Fund having 200 units has shown its NAV of ₹ 8.75 and ₹ 9.45 at the beginning and at the end of the year respectively. The Mutual Fund has given two options:
- **(i) Pay ₹ 0.75 per unit as dividend and ₹ 0.60 per unit as a capital gain, or**
- **(ii) These distributions are to be reinvested at an average NAV of ₹ 8.65 per unit.**
- **(iii) What difference it would make in terms of return available and which option is preferable?** **[2+4+1]**

Answer:
(i) Returns for the year:

(All changes on a Per -Unit Basis)

Change in Price: ₹ 9.45 - ₹ 8.75 =	₹ 0.70
Dividends received:	₹ 0.75
Capital gains distribution	₹ 0.60
Total reward	₹ 2.05

Holding period reward: ₹ 2.05 / ₹ 8.75 = 23.43%

(ii) When all dividends and capital gains distributions are re-invested into additional units of the fund @ (₹ 8.65/unit)
Dividend + Capital Gains per unit
= ₹ 0.75 + ₹ 0.60 = ₹ 1.35
Total received from 200 units = ₹ 1.35 x 200 = ₹ 270/-.
Additional Units Acquired:
= ₹ 270/₹ 8.65 = 31.21 Units.
Total No. of Units = 200 units + 31.21 units
= 231.21 units.
Value of 231.21 units held at the end of the year
= 231.21 units x ₹ 9.45 = ₹ 2,184.93
Price Paid for 200 Units at the beginning of the year
= 200 units x ₹ 8.75 = ₹ 1,750.00
Holding Period Reward
₹ (2,184.93 – 1,750.00) = ₹ 434.93
% of Holding Period Reward: ₹ 434.93/ ₹ 1,750.00 = 24.85%

(iii) Conclusion: Since the holding period reward is more in terms of percentage in option-two i.e., reinvestment of distributions at an average NAV of ₹ 8.65 per unit, this option is preferable.

(b) Given below is information of market rates of returns and data from two companies X and Y:

%

	Year 2011-12	**Year 2012-13**	**Year 2013-14**
Market	**12.0**	**11.0**	**9.0**
Company X	**13.0**	**11.5**	**9.8**
Company Y	**11.0**	**10.5**	**8.5**

Required: Determine the beta coefficients of the shares of Company X and Company Y. [6]

Answer:

Determination of Beta Coefficients of the Shares of Company X and Company Y

Company X

Year	R_X	R_m	$(R_X - \bar{R}_X)$	$(R_m - \bar{R}_m)$	$(R_X - \bar{R}_X)(R_m - \bar{R}_m)$	$(R_m - \bar{R}_m)^2$
1	13.0	12.0	1.57	1.33	2.09	1.77
2	11.5	11.0	0.07	0.33	0.02	0.11
3	9.8	9.0	-1.63	-1.67	2.72	2.79
	$\Sigma R_X = 34.3$	$\Sigma R_m = 32.0$			$\sum(R_X - \bar{R}_X)(R_m - \bar{R}_m) = 4.83$	$\sum(R_m - \bar{R}_m)^2 = 4.67$

$\bar{R}_X$	= ΣR_X / n	= 34.3 / 3	= 11.43%
$\bar{R}_m$	= ΣR_m / n	= 32.0/ 3	= 10.67%
σ_m^2	$= \frac{\Sigma(R_m - \bar{R}_m)^2}{n-1}$	$= \frac{4.67}{2}$	= 2.335
$COV_{X,m}$	$= \frac{\sum(R_X - \bar{R}_X)(R_m - \bar{R}_m)}{n-1}$	$= \frac{4.83}{2}$	= 2.415
β_X	$= \frac{CoV_{X,m}}{\sigma_m^2}$	$= \frac{2.415}{2.335}$	= 1.034

Company Y

Year	R_Y	R_m	$(R_Y - \bar{R}_Y)$	$(R_m - \bar{R}_m)$	$(R_Y - \bar{R}_Y)(R_m - \bar{R}_m)$	$(R_m - \bar{R}_m)^2$
1	11.0	12.0	1.00	1.33	1.33	1.77
2	10.5	11.0	0.50	0.33	0.17	0.11
3	8.5	9.0	-1.50	-1.67	3.17	2.79
	ΣR_Y = 30	ΣR_m = 32			$\sum(R_Y - \bar{R}_Y)(R_m - \bar{R}_m)$ = 4.67	$\sum(R_m - \bar{R}_m)^2$ = 4.67

$\bar{R}_Y$	= ΣR_Y / n	= 30 / 3	= 10.00%
$\bar{R}_m$	= ΣR_m / n	= 32/ 3	= 10.67%
σ_m^2	$= \frac{\Sigma(R_m - \bar{R}_m)^2}{n-1}$	$= \frac{4.67}{2}$	= 2.335
$COV_{Y,m}$	$= \frac{\Sigma(R_Y - \bar{R}_Y)(R_m - \bar{R}_m)}{n-1}$	$= \frac{4.67}{2}$	= 2.335
B_Y	$= \frac{CoV_{Y,m}}{\sigma_m^2}$	$= \frac{2.335}{2.335}$	= 1.00

(c) There are some criticisms of Technical Analysis in the field of Stock Market Analysis. State those criticisms. [4]

Answer:

Criticisms of Technical Analysis:

i) Difficult in interpretation: Technical analysis is not as simple as it appears to be. While the charts are fascinating to look at, interpreting them correctly is very difficult. It is always easy to interpret the charts long after the actual point of time. As such, fundamentals argue that charting techniques are no different from palmistry.

ii) Frequent changes: With changes in market, chart patterns keep on changing. Accordingly, technical analysts change their opinions about a particular investment very frequently. One day they put up a buy signal. A couple of weeks later, they see a change pattern and put up a sell signal.

iii) Unreliable changes: Changes in market behaviour observed and studied by technical analyst may not always be reliable owing to ignorance or intelligence or manipulative tendencies of some participants.

iv) Judgemental Bias: A false piece of information or wrong judgment may result in trade at a lower than market price. If the technicians fail to wait for confirmation, they incur losses.

(d) Write a short note on Types of Mutual Fund Schemes (answer should be restricted to Open Ended Funds, Close Ended Funds and Income Oriented Funds only). [3]

Answer:

Open Ended Funds: In open-ended funds, there is no limit to the size of the funds. Investors can invest as and when they like. The purchase price is determined on the basis of Net Asset Value (NAV). NAV is the market value of the fund's assets divided by the number of outstanding shares/ units of the fund.

Close Ended Funds: These funds are fixed in size as regards the corpus of the fund and the number of shares. In close ended funds, no fresh units are created after the original offer of the scheme expires. The shares/units of these funds are not redeemable at their NAV during their life as are in the case of open ended funds. The shares of such funds are traded in the secondary market on stock exchanges at market prices that may be above or below their NAV.

Income Oriented Funds: These funds offer a return much higher than the bank deposits but with less capital appreciation. The emphasis being on regular returns, the pattern of investments in general is oriented towards fixed income yielding securities like non-convertible debentures of consistently good dividend paying companies, etc.

SECTION II (40 Marks)

(Corporate Laws)

Answer Question No.5 (compulsory) and also answer any two from the rest in this Section.

Question 5.

(a) Fill in the Blanks in the following sentences by using appropriate word(s)/ phrase(s)/ number(s): [1x6=6]

(i) The ________________ has the power to fill up the casual vacancy caused in the Board.

(ii) __________________ includes any notice, circular, advertisement or other document inviting offers from the public for the subscription or purchase of any securities of a body corporate.

(iii) A company may purchase its own shares or other specified securities [called as buy back] out of its free reserves, or the ____________________ or the proceeds of any shares or other specified securities.

(iv) In the context of classification of risks, contract risks will fall under _______________ risk.

(v) In case of demerger, the company or trust that ceases to own the entity is known as the ____________________.

(vi) Under RTI Act, __________________ means a person other than the citizen making a request for information and includes a public authority.

Answer:

(i) Board of Directors
(ii) Prospectus
(iii) securities premium account
(iv) legal
(v) demerging entity
(vi) third party.

(b) Choose the most appropriate one from the stated options and write it down (only indicate A, B, C or D as you consider correct): [1×4]

(i) Which of the following committee set up by SEBI had submitted its report in February, 2003 on Corporate Governance?
(A) Narasimham Committee
(B) Kumar Mangalam Birla Committee
(C) Narayana Murthy Committee
(D) Naresh Chandra Committee.

(ii) The Competition Commission shall consist of a chairperson and not less than two but not more than _______ other members to be appointed by the Central Government. (Fill in the gap from the below.)
(A) 7
(B) 10
(C) 5
(D) 6.

(iii) Which of the following is not the content of Memorandum of Association?
(A) Name clause;
(B) Consideration clause;
(C) Object clause;
(D) Capital clause.

(iv) Which of the following is a type of Shareholders' Meeting?
(A) Annual General Meeting;
(B) Statutory Meeting;
(C) Extra-ordinary General Meeting;
(D) All of the above.

Answer:

(i) (C)
(ii) (D)
(iii) (B)
(iv) (D)

Question 6.

(a) A Ltd. was incorporated with 10 members (A to J). On 1st April 2013, the number of members reduced to 6. The debts of the company on that date were ₹ 3,00,000. On 1st Jan 2014, the number of members increased to 9. The debts of the company increased to ₹ 4,50,000 and ₹ 4,80,000 on 30th September 2013 and on 31st December 2013 respectively. Out of six members, two members, Mr. A and Mr. D were not aware of the fact that the number of members reduced to 6. Discuss the legal position. [3]

Answer:

As per section 45 of the Companies Act, 1956 if any company carries on business for more than 6 months with the number of members reduced below the statutory requirement (i.e. 2 in case of private company and 7 in case of public company), every person who was member of the company during the time when it carried on business after those 6 months and who was aware of this fact, shall be personally liable for all debts of the company contracted after those 6 months.

Accordingly, in the given case, four members (other than Mr. A and Mr. D), who were aware of reduction in number of members are personally liable for ₹ 30,000 (₹ 4,80,000 – ₹ 4,50,000) contracted after those 6 months.

(b) Ms. Suchanda has entered into a transaction with Glamour Ltd. for a contract value of ₹ 40 lacs. The Articles of Association enjoin that contracts above ₹ 10 lacs should be approved in Board Meeting. Mr. Dhuruv, an officer of the company, produces forged documents to her, which show a resolution having been passed in a Board Meeting approving the contract. Later, the forgery comes to light. Ms. Suchanda pleads that she is protected by the Doctrine of Indoor Management. — Discuss. [6]

Answer:

Doctrine of Indoor Management:

The Doctrine of Constructive Notice protects a company from outsiders. There is one limitation to that doctrine. The Doctrine of Indoor Management is an exception to the Doctrine of Constructive Notice. The Doctrine of Constructive Notice provides that an outsider must read the Memorandum and Articles of a company. But he is not expected to do more. As far as internal procedures are concerned, an outsider is entitled to presume that everything has been done according the procedures laid down and there is no irregularity. An outsider cannot find out what is going inside the doors as the doors of the management are closed to an outsider. Therefore protection to such an outsider becomes necessary. Thus while the Doctrine of Constructive Notice is a protection to the company against an outsider, the Doctrine of Indoor Management is protection to the outsiders against the company.

In certain exceptional situations, the doctrine of indoor management is not applicable. The doctrine of indoor management is not applicable where a person relies upon a document that turns out to be a forged since nothing validate forgery. A company cannot be held liable for forgeries committed by its officers.

Thus Ms. Suchanda will not succeed in her pleading.

(c) State the provisions of section 157 of the Companies Act, 1956 regarding the foreign register. [6]

Answer:

Section 157 of the Companies Act, 1956 makes provisions regarding the foreign register. The provisions are as follows:

- A company, which has a share capital or which has issued debentures may, if so authorized by its articles, keep in any State or country outside India, a branch register of members or debenture holders resident in that State or country. This register is called as a foreign register in this Act.
- The company shall within thirty days from the date of the opening of any foreign register, file with the Registrar notice of the situation of the office, where such register is kept and in the event of any change in the situation of such office or of its discontinuance, as the case may be, file notice with the Registrar of such change or discontinuance. [Section 157 (2) of the Companies Act, 1956].
- In case of any default made in complying with the requirements of the above sub section (2), the company and every officer of the company who is in default, shall be punishable with fine which may extend to ₹ 500 for every day during which the default continues.
- A foreign register shall be deemed to be part of the company's register of members or of debenture holders as the case may be. [Section 158 (1) of the Companies Act, 1956].
- A foreign register shall be kept, shall be open to inspection and may be closed, and extracts may be taken there from and copies thereof may be required as per the relevant provisions of the Act. A newspaper advertisement should be given before the register is closed. [Section 158 (2) of the Companies Act, 1956].
- Subject to the provisions of the Act, a company may by its articles make such regulations as it thinks fit in regard to its foreign registers.

Question 7.

(a) List the powers of the liquidator in a winding up by the Tribunal (with the sanction of the Tribunal). [6]

Answer:

Section 457 (1) of the Companies Act, 1956, provides that the liquidator in a winding up by the Tribunal shall have the following powers, with the sanction of the Tribunal:

(i) To institute or defend any suit, prosecution, or other legal proceeding, civil or criminal, in the name and on behalf of the company.
(ii) To carry on the business of the company so far as may be necessary for the beneficial winding up of the company.
(iii) To sell the immovable and movable property and actionable claims of the company by public auction or private contract, with power to transfer the whole thereof to any person or body corporate, or to sell the same in parcels.
(iv) To sell whole of the undertaking of the company as a going concern.
(v) To raise on the security of the assets of the company any money requisite.
(vi) To do all such other things as may be necessary for winding up the affairs of the company and distributing of its assets.

(b) "Synergy takes the form of revenue enhancement and cost savings." — describe the advantages of synergy to the companies. [4]

Answer:
By synergy, the companies hope to benefit from the following:

- Staff reductions - As every employee knows, mergers tend to mean job losses. Consider all the money saved from reducing the number of staff members from accounting, marketing and other departments. Job cuts will also include the former CEO, who typically leaves with a compensation package.

- Economies of scale - Whether it's purchasing stationery or a new corporate IT system, a bigger company placing the orders can save more on costs. Mergers also translate into improved purchasing power to buy equipment or office supplies— when placing larger orders, companies have a greater ability to negotiate price with their suppliers.

- Acquiring new technology - To stay competitive, companies need to stay on top of technological developments and their business applications. By buying a smaller company with unique technologies, a large company can keep or develop a competitive edge.

- Improved market reach and industry visibility - Companies buy companies to reach new markets and grow revenues and earnings. A merge may expand two companies' marketing and distribution, giving them new sales opportunities. A merger can also improve a company's standing in the investment community: bigger firms often have an easier time raising capital than smaller ones.

(c) A shareholder living in Kolkata sent a transfer deed for registration of transfer of shares in a company having its registered office in Mumbai. The share certificates duly endorsed in his name were not received by him even after the expiry of four months from the date of lodgment. He lodged a criminal complaint before the appropriate court dealing with economic offences at Kolkata. Can the Court in Kolkata entertain the complaint? [5]

Answer:
According to section 113(1) of the Companies Act, 1956, every company, unless prohibited by any provision of law or of any order of court, tribunal or other authority, shall within two months after the application for the registration of transfer of any such shares, deliver the certificates of all shares transferred. In the case of a listed company under the listing agreement this period has been reduced to 30 days.

The facts of the given case are similar to H.V. Jayaram v. ICICI Ltd. 1999 (7) Scale 481. In this case the special court for Economic Offences in the State of Karnataka rejected the appellant's complaint against the respondent company on the ground that since the company had its registered office at Mumbai it is only the court which has territorial jurisdiction over the registered office of the company that can entertain the petition and not the court located in the State of Karnataka where the shareholder is residing. The High Court also upheld the order of the Special Court. On appeal Supreme Court held the cause of action for failure to deliver share certificate arises where the registered office of the company is situated and not in the jurisdiction of the Court located in the place where the complainant resides.

Accordingly in the present case also, the court in Kolkata cannot entertain the complaint against a company having its registered office in Mumbai.

Question 8.

(a) Shakshi Telecom Ltd., a private mobile operator had furnished confidential information relating to customer complaints lodged with the company during the quarter ended 31.03.2014 to a public authority. On an application under the Right to Information Act, 2005, the public authority wants to furnish the said information. The authority seeks the objections of Shakshi Telecom Ltd. Can Shakshi Telecom Ltd. ask the public authority not to furnish the same on the grounds that the said information is confidential and that it may endanger its image in the market? What decision should the public authority take? [5]

Answer:
Disclosure of Information treated as confidential by third party:
As per section 11(1) of the Right to Information Act, 2005 where a public authority intends to disclose any information or record, or part thereof on a request made under this Act which relates to, or has been supplied by a third party and has been treated as confidential by that third party, the Public Information Officer shall, within five days from the receipt of a request, give written notice to such third party of the request and of the fact that the public authority intends to disclose the information or record, or part thereof and invite the third party to make a submission, in writing or orally, regarding whether the information should be disclosed, which submission shall be taken into account when determining whether to disclose the information.

Provided that except in the case of trade or commercial secrets protected by law, disclosure may be allowed if the public interest in disclosure outweighs in importance any possible harm or injury to the interests of such party.

Shakshi Telecom Ltd. cannot ask the public authority not to furnish the same on the grounds that the said information is confidential and that it may spoil its image in the market. This is not trade or commercial secrets protected by law. Hence the public authority should overrule the objections of Shakshi Telecom Ltd. and furnish the information to the applicant under the RTI Act.

(b) Write down the characteristics of a company (any five). [5]

Answer:
The characteristics of a company:

(i) Incorporated association: A company is incorporated or registered under Companies Act. Minimum number of members required is seven in case of Public Ltd. Company and two in case of Private Ltd. Company, for the purpose of registration.

(ii) Separate Entity: it has a separate legal status from its members or shareholders. The property of the company is not the property of the shareholders. Similarly shareholders may come and go but a company remains as it is.

(iii) Artificial person: A company is a juristic person and exits only under contemplation of law. Being an artificial person it has to depend on it's natural representatives such as directors, officers, shareholders who work on behalf of the company within their scope of authority and bind the company with their actions.

(iv) Perpetual Succession and Common Seal: A company has a perpetual succession. It is created by a process of law and it ceases to exist by the process of law only. It has a common seal. In other words a company is an artificial person created by law and all that a person can do, a company can do under its common seal.

(v) Capital: A company is incorporated with an authorized share capital, which is the maximum amount of share capital, which can be raised by it in its lifetime unless it is changed subsequently. Out of this authorized share capital, some amount of capital as per the needs of the company is offered to the members of the public. The amount of capital is divided into small parts, which are called as shares.

(vi) Transferability of Shares: The shares of a company are freely transferable in case of a public limited company. In case of a private limited company, the shares are not freely transferable.

(vii) Limited Liability: the liability of members of the shareholders of a limited company is limited. This means that if the face value of a share is ₹ 100 and a shareholder has purchased 10 such shares, the total value of the holding will be ₹ 1000. Once this amount is paid by the shareholder, he need not pay an additional amount even at the time of winding up of the company.

(viii) Capacity to sue and to be sued: A company is an artificial person created by law. It has a capacity to sue others in case of any offence committed against it. Similarly it can be sued by others if it has committed any offence against any party.

(c) What is Project Management? State the benefits of Project governance. [1+4]

Answer:

Project Management: it is the discipline of planning, organizing, and managing resources to bring about the successful completion of specific project goals and objectives. The primary challenge of project management is to achieve all of the project goals and objectives while secondary challenge is to optimize the allocation and integration of inputs necessary to meet pre-defined objectives.

Benefits of Project governance:

Project governance will:

1) Outline the relationships between all internal and external groups involved in the project
2) Describe the proper flow of information regarding the project to all stakeholders
3) Ensure the appropriate review of issues encountered within each project
4) Ensure that required approvals and direction for the project is obtained at each appropriate stage of the project.