Skillshort

Self-Study Preparation Pack

CMA INTERMEDIATE

Paper 5: Business Laws and Ethics (BLE)

Chapter-wise Detailed Notes

For the December 2026 term (Thu 10 Dec 2026, 2–5 pm) and June 2027 · ICMAI Syllabus 2022 · Companies Act and other laws as amended up to 31 May 2026 (ICMAI clarification of 15-09-2026)

100 marks · 3 hours | Q1: 15 MCQs × 2 = 30 | Any 5 of Q2–Q8 × 14 = 70 | Companies Act 40% · Commercial laws 30%

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This subject pack has 6 parts

1 Chapter-wise notes
2 Important topics & weightage
3 Past papers: trends & links
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Prepared by Skillshort for self-study. Original explanations and questions; not an official ICAI/ICMAI/ICSI publication. Items marked VERIFY should be checked against the latest official material.

How to use these notes

These notes follow the **ICMAI Syllabus 2022 module order** (13 modules in 4 sections; the Companies Act module is split into Chapters 9–19). Each chapter gives the law section by section, comparison tables and the points that examiners reward. Read a chapter, then solve its set in file 05. Use the formula and number sheet at the end for last-week revision.

Paper at a glance

Item	Detail
Marks / time	100 marks, 3 hours, offline at exam centres, 2:00–5:00 pm
Section A (compulsory)	Q1 – **15 MCQs × 2 marks = 30** across all modules; no negative marking VERIFY
Section B	**Any 5 of Q2–Q8**, 14 marks each (usually two 7-mark parts) = 70
ICMAI study weightage	Commercial laws **30%** (Law and legal system 5, Contract 10, Sale of Goods 5, NI 5, Partnership and LLP 5) · Industrial laws **15%** (Factories, Gratuity, EPF, ESI 10; Code on Wages 5) · Companies Act **40%** · Business ethics **15%**
Applicable law for December 2026	Companies Act, 2013 with rules, notifications and circulars, and other laws, as amended up to **31 May 2026** (ICMAI Ref DoS-Academics/09/2026)

EXAM TIP How marks are given in law answers

Write **Provision → Analysis of facts → Conclusion** for case questions. For theory questions, number the points and put the section number in the first line. A 7-mark part needs about 7 clear points, not a long essay.

NOTE Labour codes

The four labour codes (Code on Wages, Industrial Relations, Social Security, and Occupational Safety, Health and Working Conditions) were brought into force by the Government with effect from **21 November 2025** VERIFY. The ICMAI syllabus still lists the Factories Act, Gratuity Act, EPF Act and ESI Act. Learn them as given in the ICMAI study material and supplementary, and check the December 2026 supplementary for Paper 5 before the exam.

Chapter 1: Introduction to Law and the Legal System in India

1.1 Meaning and sources of law

Law is a body of rules, recognised and enforced by the State, that regulates the conduct of persons in society. It gives certainty, protects rights, settles disputes and sets the framework within which business operates.

Source of law	Meaning
Customs	Long-standing, reasonable, certain and continuous practices accepted as binding. Must not be against public policy or statute
Judicial precedent	Decisions of higher courts bind lower courts (*stare decisis*). Supreme Court decisions bind all courts in India (Art. 141)
Legislation	Law made by Parliament or State legislatures – the most important modern source; includes delegated (subordinate) legislation
Personal law	Religious texts and commentaries for personal matters (marriage, succession)
Equity, justice and good conscience	Where no law applies, courts decide on fairness

1.2 The Constitution of India and Fundamental Rights

The Constitution is the **supreme law**; it came into force on **26 January 1950**. The Preamble declares India a **sovereign, socialist, secular, democratic republic** and secures justice, liberty, equality and fraternity. India has a **federal structure with a strong Centre** (quasi-federal): the Seventh Schedule divides subjects into the **Union List, State List and Concurrent List**.

Fundamental Right (Part III)	Articles	Key points
Right to equality	14–18	Equality before law (14); no discrimination on religion, race, caste, sex, place of birth (15); equal opportunity in public employment (16); abolition of untouchability (17) and titles (18)
Right to freedom	19–22	Six freedoms of citizens in Art. 19 – speech and expression, assembly, association, movement, residence, **profession, occupation, trade or business** – subject to reasonable restrictions; protection in respect of conviction (20); life and personal liberty (21); education 6–14 years (21A); arrest and detention (22)
Right against exploitation	23–24	No traffic in human beings or forced labour (23); no child below 14 in factories, mines or hazardous work (24)
Right to freedom of religion	25–28	Freedom of conscience and religion
Cultural and educational rights	29–30	Protection of minorities' interests; right of minorities to run educational institutions
Right to constitutional remedies	32	Move the Supreme Court for enforcement – writs of **habeas corpus, mandamus, prohibition, certiorari and quo warranto**; High Courts issue writs under Art. 226

NOTE Directive Principles and Fundamental Duties

Directive Principles of State Policy (Part IV, Art. 36–51) guide the State in making laws (e.g., equal pay for equal work, living wage) but are **not enforceable** in courts. **Fundamental Duties** (Art. 51A) were added by the 42nd Amendment, 1976.

1.3 Primary and subordinate legislation

- **Primary legislation** – Acts passed by Parliament or a State legislature (e.g., the Companies Act, 2013).
- **Subordinate (delegated) legislation** – rules, regulations, bye-laws, notifications and orders made by the executive under powers given by an Act (e.g., Companies (Incorporation) Rules, 2014). It must be within the powers of the parent Act; otherwise it is **ultra vires** and void.

- Reasons for delegation: lack of parliamentary time, technical matters, flexibility, emergencies. Controls: **parliamentary control** (laying before the House), **judicial control** (ultra vires review) and **procedural control** (publication, consultation).

1.4 Legislative process in India

Stage	What happens
Introduction / first reading	A bill is introduced in either House (a **Money Bill** only in the Lok Sabha, on the President's recommendation – Art. 110, 117)
Second reading	General discussion; may be referred to a select or joint committee; clause-by-clause consideration
Third reading	Bill is passed or rejected as a whole
Other House	Same three stages; disagreement on an ordinary bill → **joint sitting** (Art. 108). For a Money Bill the Rajya Sabha may only recommend within **14 days**
President's assent	Art. 111 – assent, withhold, or return (not a Money Bill) for reconsideration once

Kinds of bills: ordinary, money (Art. 110), financial (Art. 117) and **constitutional amendment** bills (Art. 368 – special majority).

1.5 Structure of courts and legal methods

- **Supreme Court** (Art. 124) – original, appellate, advisory (Art. 143) and writ jurisdiction (Art. 32); its law binds all courts (Art. 141).
- **High Courts** (Art. 214) – writ jurisdiction (Art. 226), supervision of subordinate courts (Art. 227).
- **District and subordinate courts**; **tribunals** – NCLT/NCLAT, ITAT, SAT, consumer commissions.
- Legal methods: **interpretation** of statutes (literal, golden, mischief rules), use of **precedent**, and **legal reasoning** from facts to law.

1.6 Alternative Dispute Resolution (ADR)

ADR settles disputes **outside courts** – it is faster, cheaper, private and less formal. Section 89 of the Code of Civil Procedure, 1908 lets courts refer disputes to ADR.

Mode	Meaning
Arbitration	A neutral arbitrator gives a **binding award** – Arbitration and Conciliation Act, 1996. The award is enforced like a court decree; limited grounds for challenge (s. 34)
Conciliation	A conciliator helps parties reach a settlement; the settlement agreement signed by parties is binding (Part III of the 1996 Act)
Mediation	A neutral mediator facilitates a voluntary settlement – Mediation Act, 2023 VERIFY
Negotiation	Parties settle directly without a third party
Lok Adalat	"People's court" under the Legal Services Authorities Act, 1987; award is **final and binding**, no appeal, no court fee

1.7 Legal terminology and maxims

Maxim	Meaning
Ignorantia juris non excusat	Ignorance of law is no excuse
Ubi jus ibi remedium	Where there is a right, there is a remedy
Audi alteram partem	Hear the other side (natural justice)
Nemo judex in causa sua	No one should be a judge in his own cause
Res judicata	A matter finally decided cannot be re-litigated
Caveat emptor	Let the buyer beware
Nemo dat quod non habet	No one can give what he does not have
Quantum meruit	As much as is earned
Ex turpi causa non oritur actio	No action arises from an immoral cause

Maxim	Meaning
Volenti non fit injuria	No injury to one who consents
Actus non facit reum nisi mens sit rea	An act is not guilty unless the mind is guilty
Ratio decidendi / obiter dicta	The binding reason for a decision / remarks by the way (not binding)
Ultra vires	Beyond powers
Bona fide / mala fide	In good faith / in bad faith

Chapter 2: The Indian Contract Act, 1872 – General Principles

2.1 Introduction

The **Indian Contract Act, 1872** came into force on **1 September 1872** and extends to the whole of India. It lays down the general principles of contract (Sections 1–75) and special contracts – indemnity, guarantee, bailment, pledge and agency (Sections 124–238). Sale of goods and partnership, originally part of the Act, are now governed by separate Acts.

2.2 Important definitions – Section 2

Section	Term	Meaning (in simple words)
2(a)	Proposal / offer	When one person signifies to another his willingness to do or not to do something, with a view to obtaining that person's assent
2(b)	Acceptance / promise	When the person to whom the proposal is made signifies his assent; a proposal when accepted becomes a promise
2(c)	Promisor and promisee	Person making the proposal is the promisor; person accepting is the promisee
2(d)	Consideration	Something done, abstained from, or promised at the desire of the promisor, by the promisee or any other person
2(e)	Agreement	Every promise and every set of promises forming consideration for each other
2(g)	Void agreement	An agreement not enforceable by law
2(h)	Contract	An agreement enforceable by law
2(i)	Voidable contract	Enforceable at the option of one party but not of the other
2(j)	Void contract	A contract which ceases to be enforceable

√x FORMULA Contract

Contract = Agreement + Enforceability by law

Agreement = Offer + Acceptance

REMEMBER **"All contracts are agreements, but all agreements are not contracts." Social and domestic agreements (e.g. promise to go to a movie) are not contracts because there is no intention to create legal relations.**

2.3 Essentials of a valid contract (Sec 10)

1. **Offer and acceptance** – two or more parties; lawful offer and lawful acceptance.
2. **Intention to create legal relations** – *Balfour v. Balfour* (1919): husband's promise to pay monthly allowance to wife was a domestic arrangement, not a contract.
3. **Lawful consideration** – something in return (Sec 23).
4. **Capacity of parties** – competent to contract (Sec 11).
5. **Free consent** – not caused by coercion, undue influence, fraud, misrepresentation or mistake (Sec 14).
6. **Lawful object** – not forbidden by law, fraudulent, injurious, immoral or against public policy.
7. **Not expressly declared void** (Secs 24–30, 56).
8. **Certainty of meaning** (Sec 29).
9. **Possibility of performance** (Sec 56).
10. **Legal formalities** – writing, registration where required by law.

2.4 Offer (proposal)

Types of offer

Type	Meaning	Example
Express offer	By words, spoken or written	Email offering to sell a laptop for ₹40,000
Implied offer	By conduct	Bus running on a route offers to carry passengers
Specific offer	Made to a definite person	A offers to sell his car to B
General offer	Made to the public at large; anyone fulfilling the conditions can accept	*Carlill v. Carbolic Smoke Ball Co.* (1893) – reward of £100
Cross offer	Two identical offers cross each other in post	No contract – no acceptance
Counter offer	Acceptance with changed terms	Rejects the original offer – *Hyde v. Wrench*
Standing / continuing offer	Open for a period; tender for supply as required	Supply of goods "as and when ordered"

Rules of a valid offer

- Must intend to create legal relations.
- Terms must be definite and certain.
- Must be **communicated** to the offeree – *Lalman Shukla v. Gauri Dutt* (1913): servant who found the boy without knowing of the reward could not claim it.
- Must be distinguished from an **invitation to offer** – price tags in shops, catalogues, advertisements, auction announcements, tenders, timetable (*Pharmaceutical Society v. Boots Cash Chemists*; *Harvey v. Facey*).
- May be conditional; but cannot say silence will amount to acceptance (*Felthouse v. Bindley*).

Lapse / revocation of offer (Sec 6)

By notice of revocation, lapse of prescribed or reasonable time, failure to fulfil a condition precedent, death or insanity of the offeror (if known to offeree before acceptance), counter offer, rejection, or subsequent illegality.

2.5 Acceptance

- Must be **absolute and unqualified** (Sec 7) – mirror image of the offer.
- Expressed in the usual and reasonable manner, or the prescribed manner.
- Must be **communicated** to the offeror; mental acceptance is not enough – *Brogden v. Metropolitan Railway* (acceptance by conduct).
- Given by the offeree or his authorised agent, while the offer is still in force.
- Cannot precede the offer.

Communication when complete (Sec 4)

Communication of	Complete as against the offeror	Complete as against the acceptor
Offer	When it comes to the knowledge of the offeree	–
Acceptance	When it is put in the course of transmission (posted)	When it comes to the knowledge of the offeror
Revocation	As against the person making it – when put in course of transmission; as against the recipient – when it comes to his knowledge	

Revocation of offer is possible before the communication of acceptance is complete against the offeror (i.e. before the letter of acceptance is posted). **Revocation of acceptance** is possible before acceptance reaches the offeror (Sec 5).

WORKED EXAMPLE **Postal rules**

A posts an offer to B on 1 March, received on 3 March. B posts acceptance on 4 March; it reaches A on 6 March.

A can revoke his offer before 4 March (when B posts). B can revoke acceptance before 6 March (by a faster means, e.g. phone). After 6 March, the contract is binding on both.

Electronic contracts are valid under the **IT Act, 2000** (Sec 10A); acceptance by email or click is complete when it enters the offeror's system.

2.6 Consideration

"Something in return" – *quid pro quo*. Consideration may be past, present or future.

Rules

- Must move at the **desire of the promisor** – *Durga Prasad v. Baldeo* (building a market at the Collector's desire, not the promisor's – no consideration).
- May move from the **promisee or any other person** – *Chinnaya v. Ramayya* (1882): consideration by a third person valid. (Different from English law.)
- Need **not be adequate**, but must be **real** and something of value in the eye of law (Sec 25, Expl. 2).
- Must not be illegal, immoral or opposed to public policy (Sec 23).
- Performance of an existing legal duty is not consideration.

Privity of contract

A stranger to the contract cannot sue (*Dunlop Pneumatic Tyre Co. v. Selfridge*, 1915), but a stranger to consideration can. **Exceptions**: trust beneficiary, marriage settlement/partition provisions, acknowledgement or estoppel, assignment, covenant running with land, agent.

No consideration, no contract – exceptions (Sec 25)

1. Agreement in writing and registered, made out of **natural love and affection** between near relatives.
2. Promise to **compensate a person** who has already voluntarily done something for the promisor (past voluntary service).
3. Written and signed promise to pay a **time-barred debt**.
4. Completed gift (Sec 25 explanation 1).
5. Agency (Sec 185) – no consideration needed to create agency.
6. Bailment without charge (gratuitous bailment).
7. Contribution to charity – where the promisee has acted on the promise (*Kedarnath v. Gorie Mohammed*).

LEGAL PROVISION **Exceptions to privity of contract**

A stranger to a contract cannot sue, **except**: (1) beneficiary under a **trust** or charge; (2) **marriage settlement, partition or family arrangement** providing for a person; (3) **acknowledgement or estoppel** – the promisor by conduct recognises the third party's right; (4) **assignment** of rights under a contract; (5) **covenant running with land** – a buyer of land with notice is bound by the covenant; (6) contracts entered into through an **agent**.

WORKED EXAMPLE **Natural love and affection – Sec 25(1)**

Abeer gives an iPhone to his friend Chhaya on her birthday. A **completed gift** is valid without consideration (Sec 25 Explanation 1). A *promise* to give without consideration is enforceable only if it is **written, registered** and made out of **natural love and affection** between parties standing in a **near relation** (husband–wife, parent–child), not between friends.

2.7 Capacity to contract

Every person is competent who is of the age of majority, of sound mind, and not disqualified by law.

Minor's agreements

A **minor** (below 18 years; 21 if a guardian appointed by court) – an agreement with a minor is **void ab initio** – *Mohori Bibee v. Dharmodas Ghose* (1903).

- No ratification on attaining majority.
- No estoppel against a minor – he can plead minority even if he lied about age.
- Minor can be a **promisee/beneficiary** (e.g. payee of a cheque).
- Liability for **necessaries** supplied to a minor – from his property, not personally (Sec 68).
- Minor can be admitted to the **benefits of a partnership** (Sec 30 of Partnership Act).
- Minor's parents not liable unless they authorised the agent.
- Restitution – if a minor obtains goods by fraud, court may order return of goods if traceable.

Persons of unsound mind (Sec 12)

A person who is usually of unsound mind but occasionally sound may contract when of sound mind; a usually sound person may not contract when temporarily unsound (drunk, delirious). Agreements are void.

Persons disqualified by law

Alien enemies (during war), foreign sovereigns and diplomats (cannot be sued without consent), convicts during imprisonment, insolvents, companies beyond MOA powers.

2.8 Free consent

Two persons are said to **consent** when they agree upon the same thing in the same sense (*consensus ad idem*). Consent is **free** when not caused by:

Factor	Section	Meaning	Effect
Coercion	15	Committing or threatening any act forbidden by the Indian Penal Code (now Bharatiya Nyaya Sanhita), or unlawfully detaining property, to make a person enter into an agreement	Voidable (Sec 19)
Undue influence	16	One party in a position to dominate the will of the other uses it to obtain unfair advantage (doctor–patient, guardian–ward, teacher–student)	Voidable (Sec 19A); court may set aside on terms
Fraud	17	Intentional false representation or active concealment to deceive	Voidable; can also claim damages
Misrepresentation	18	Innocent false statement believed to be true	Voidable; no damages
Mistake of fact – bilateral	20	Both parties mistaken about an essential fact	**Void**
Mistake of fact – unilateral	22	Only one party mistaken	Not voidable (generally valid)
Mistake of Indian law	21	Ignorance of law is no excuse	Valid
Mistake of foreign law	21	Treated as mistake of fact	Void (if bilateral)

REMEMBER Mere **silence** is not fraud, except where there is a duty to speak (e.g. insurance – ***uberrimae fidei***), or silence is equivalent to speech.

WORKED EXAMPLE **Coercion vs undue influence**

(a) A threatens to shoot B unless B sells his house to A for ₹5 lakh. → Coercion; B can avoid the contract.

(b) A spiritual guru persuades his devotee to gift all his property to the guru for "salvation". → Undue influence; contract voidable at devotee's option (*Mannu Singh v. Umadat Pandey*).

LEGAL PROVISION **Undue influence (Sec 16) and coercion (Sec 15)**

A person is deemed to be in a position to **dominate the will** of another where he (a) holds **real or apparent authority** (employer–employee, income-tax officer–assessee), (b) stands in a **fiduciary relation** (doctor–patient, lawyer–client, guardian–ward), or (c) contracts with a person whose mental capacity is affected by **age, illness or distress**. Burden of proof lies on the dominant party (Sec 16(3)) where the transaction appears unconscionable.

A **threat to commit suicide** has been held to amount to **coercion** (*Chikham Amiraju v. Chikham Seshamma*) – it is forbidden by law. Effect of coercion, undue influence, fraud and misrepresentation: contract is **voidable** at the option of the aggrieved party (Sec 19, 19A).

2.9 Void agreements

Section	Void agreement
24	Consideration or object unlawful in part
25	Without consideration (subject to exceptions)
26	In **restraint of marriage** (except of minor)
27	In **restraint of trade** – except sale of goodwill (reasonable local limits), partnership restrictions
28	In **restraint of legal proceedings** – except arbitration agreements
29	Uncertain agreements
30	**Wagering** agreements – except horse race prize contests above ₹500, crossword competitions involving skill, games of skill, insurance
36	Contingent on impossible events
56	Agreement to do an impossible act

Void vs voidable

Basis	Void agreement	Voidable contract
Validity	Void from the beginning	Valid until avoided by aggrieved party
Cause	Lack of essential element (consideration, object, capacity)	Lack of free consent (except mistake)
Enforcement	No one can enforce	Aggrieved party may enforce or rescind
Third party rights	No title passes	Third party in good faith gets title before rescission

LEGAL PROVISION **Agreements opposed to public policy (Sec 23)**

Trading with an enemy; trafficking in public offices; interference with the course of justice; stifling prosecution; maintenance and champerty (unfair funding of litigation); agreements tending to create interest against duty; marriage brokerage; restraint of parental rights; agreements to defraud creditors or revenue; unreasonable restraint of trade or of personal liberty.

2.10 Contingent contracts (Sec 31–36)

A **contingent contract** is a contract to do or not to do something, if some event, **collateral** to the contract, does or does not happen (Sec 31). Contracts of insurance, indemnity and guarantee are contingent contracts.

Section	Rule
32	Contract contingent on the **happening** of an uncertain future event – enforceable only when the event happens; void if it becomes impossible
33	Contingent on the event **not happening** – enforceable when its happening becomes impossible
34	If the event is the **future conduct of a living person**, it is deemed impossible when that person acts so as to make it impossible (A agrees to pay B if B marries C; C marries D – impossible)

Section	Rule
35	Event to happen within a **fixed time** – void if not happened by then; event not to happen within a fixed time – enforceable when the time expires
36	Contingent on an **impossible event** – void, whether or not the parties knew of it
Wagering vs contingent	A wager is void (Sec 30) – both parties only interested in winning/losing; a contingent contract is valid and the event is collateral

2.11 Quasi-contracts (Sec 68–72)

Obligations imposed by law to prevent unjust enrichment, even though there is no agreement.

Section	Situation	Effect
68	**Necessaries** supplied to a person incapable of contracting (minor, lunatic) or his dependants	Supplier reimbursed from the incapable person's **property** (no personal liability)
69	Payment by an **interested person** of money which another is bound to pay	Entitled to be reimbursed (e.g., paying arrears of land revenue to save one's own interest)
70	Lawfully doing a **non-gratuitous act** whose benefit another enjoys	The other must compensate or return the thing
71	**Finder of goods**	Same responsibility as a bailee
72	Money paid or thing delivered by **mistake or under coercion**	Must be repaid or returned

⚖ LEGAL PROVISION **Quantum meruit**

"As much as is earned". Where a contract is discharged by breach or becomes void after one party has done part of the work, he can claim **reasonable remuneration for the work actually done**. Conditions: the original contract is discharged/void, the claimant was not at fault, and the other party has received the benefit. Example: *Planche v. Colburn* – an author paid for chapters written though the publisher abandoned the series.

2.12 Performance and discharge of contracts

Performance

Parties must perform or offer to perform their promises (Sec 37). A valid **tender** (offer to perform) must be unconditional, at proper time and place, of the whole obligation (Sec 38). Joint promisors are jointly and severally liable (Sec 43).

Modes of discharge

Mode	Explanation
By performance	Actual performance or tender
By agreement (Sec 62–63)	**Novation** (new contract replaces old), **alteration**, **rescission**, **remission** (accepting less), **waiver**, merger
By impossibility (Sec 56)	Doctrine of **frustration** – destruction of subject matter (*Taylor v. Caldwell*), death or incapacity, change of law, outbreak of war, non-occurrence of contemplated event (*Krell v. Henry*)
By lapse of time	Limitation Act 1963 – usually 3 years
By operation of law	Death (personal contracts), insolvency, merger, unauthorised material alteration
By breach	Actual breach or anticipatory breach

Anticipatory breach (Sec 39)

When a party refuses to perform **before** the due date, the other party can treat the contract as ended immediately and sue for damages, or wait till the due date (*Hochster v. De la Tour*).

LEGAL PROVISION **Refusal to perform – Sec 39**

When a party refuses altogether to perform, or disables himself from performing his promise in its entirety, the promisee may **put an end to the contract**, unless he has by words or conduct signified acquiescence in its continuance. Effects: (1) the promisee is excused from his own performance; (2) he can sue for **damages** (Sec 75); (3) if he elects to continue, he cannot later rescind on that ground.

2.13 Remedies for breach

Remedy	Explanation
Rescission	Aggrieved party treats the contract as ended and is freed from his obligations
Damages (Sec 73)	Compensation for loss which naturally arose in the usual course, or which parties knew was likely – *Hadley v. Baxendale* (1854). Remote losses not recoverable
Liquidated damages / penalty (Sec 74)	Only reasonable compensation up to the named amount
Quantum meruit	"As much as earned" – payment for work done when contract is ended
Specific performance	Court orders actual performance where damages are inadequate (Specific Relief Act 1963 – unique property)
Injunction	Court order restraining a party from doing an act

Kinds of damages

Ordinary (general), special (if known at contract time), exemplary/vindictive (rare – breach of promise to marry, dishonour of cheque), nominal (no actual loss), and damages for inconvenience.

WORKED EXAMPLE **Hadley v. Baxendale**

A mill's crankshaft broke and was given to a carrier for delivery to the maker. The carrier delayed. The mill stopped for want of the shaft. The carrier was **not** liable for loss of profit, because he was not told that the mill would remain idle – the loss was too remote.

EXAM TIP **In case-based questions, write: (1) the relevant section, (2) the rule in one line, (3) a decided case, (4) your answer. This 4-step format scores full marks.**

LEGAL PROVISION **Penalty vs liquidated damages (Sec 74)**

1. **Liquidated damages** are a genuine pre-estimate of the loss; a **penalty** is a sum fixed *in terrorem* (to frighten) and is far above the probable loss.
2. Under Indian law the distinction is not strict: the court awards **reasonable compensation not exceeding the amount named**, whether it is called penalty or liquidated damages.
3. A stipulation for **increased interest from the date of default** may be a penalty.
4. Exception: bail bonds/securities given to Government – full amount recoverable.

Chapter 3: Special Contracts – Indemnity, Guarantee, Bailment, Pledge and Agency

3.1 Contract of indemnity (Sec 124–125)

A **contract of indemnity** is a contract by which one party promises to save the other from loss caused to him by the conduct of the promisor himself or of any other person.

- **Indemnifier** – the person who promises to make good the loss.
- **Indemnity holder (indemnified)** – the person whose loss is protected.
- Indian definition covers only loss caused by **human agency**; fire and marine insurance (accidents) are covered by general law.

Rights of indemnity holder (Sec 125)

He can recover from the indemnifier: all **damages** he is compelled to pay in a suit, all **costs** of such a suit (if he acted prudently or with authority), and all sums paid under a **compromise** of such a suit (if not contrary to orders and prudent).

> **NOTE Life insurance and indemnity**
>
> A contract of **life insurance** is not a contract of indemnity – the insurer pays a fixed sum on death or maturity irrespective of the actual loss; the loss of life cannot be measured in money. Fire and marine insurance are contracts of indemnity.

3.2 Contract of guarantee (Sec 126)

A **contract of guarantee** is a contract to perform the promise, or discharge the liability, of a third person in case of his default.

Party	Role
Surety	Gives the guarantee
Principal debtor	Whose default is guaranteed
Creditor	To whom the guarantee is given

Essentials

Three parties and three contracts; primary liability of the principal debtor; consideration (anything done for the benefit of the principal debtor is sufficient – Sec 127); consent not obtained by misrepresentation or concealment; may be oral or written.

Indemnity vs guarantee

Basis	Indemnity	Guarantee
Parties	Two	Three
Contracts	One	Three
Liability	Primary liability of indemnifier	Secondary liability of surety (arises on default)
Object	Protection from loss	Security for creditor
Right to sue third party	Indemnifier can sue only after assignment	Surety gets rights of creditor (subrogation) after paying
Existing debt	Not necessary	Necessary

Kinds of guarantee

- **Specific guarantee** – for a single debt; ends when the debt is paid.
- **Continuing guarantee (Sec 129)** – extends to a series of transactions; can be revoked for future transactions by notice (Sec 130) or by death of surety (Sec 131).

Liability of surety (Sec 128)

Co-extensive with that of the principal debtor, unless otherwise provided. The creditor can sue the surety directly without first suing the principal debtor.

Rights of surety

- **Against creditor** – right to securities held by the creditor (Sec 141); right to claim set-off.
- **Against principal debtor** – right of **subrogation** (Sec 140) and right to **indemnity** (Sec 145).
- **Against co-sureties** – right to contribution equally (Sec 146) or in proportion to amounts guaranteed (Sec 147).

Discharge of surety

By revocation (notice/death), variance in terms without consent (Sec 133), release or discharge of principal debtor (Sec 134), compounding/giving time to principal debtor without consent (Sec 135), act or omission of creditor impairing surety's remedy (Sec 139), loss of security (Sec 141), guarantee obtained by misrepresentation or concealment (Sec 142–143).

WORKED EXAMPLE Co-sureties

A, B and C are sureties for D's loan of ₹3,00,000 for ₹50,000, ₹1,00,000 and ₹1,50,000 respectively. D defaults with ₹1,20,000 unpaid.

Under Sec 147, they contribute in proportion 1 : 2 : 3 → A ₹20,000, B ₹40,000, C ₹60,000 (each within his limit).

LEGAL PROVISION Co-sureties – Sec 146 and 147

Co-sureties liable for the same debt contribute **equally** (Sec 146) unless otherwise agreed. Where they are bound in **different sums**, each pays an equal share **subject to the maximum of his own limit** (Sec 147).

```
Debt ₹4,00,000; limits A ₹1,00,000, B ₹2,00,000, C ₹4,00,000 → equal share 1,33,333: A pays 1,00,000
(limit); balance 3,00,000 shared B 1,50,000 and C 1,50,000.
Debt ₹6,00,000: equal 2,00,000 – A 1,00,000; balance 5,00,000 → B 2,00,000 (limit), C 3,00,000.
```

3.3 Bailment (Sec 148)

Bailment is the delivery of goods by one person to another for some purpose, upon a contract that they shall, when the purpose is accomplished, be returned or otherwise disposed of according to the directions of the person delivering them.

- **Bailor** – delivers goods. **Bailee** – receives goods.
- Essentials: contract, delivery of **possession** (not ownership), purpose, return of the **specific** goods. Only **movable goods**; deposit of money is not bailment.

Types

Gratuitous or non-gratuitous; for the exclusive benefit of bailor, bailee, or mutual benefit.

Duties of bailor

Disclose known faults (Sec 150); bear extraordinary expenses (Sec 158); indemnify bailee for defective title; receive back the goods.

Duties of bailee

- Take **reasonable care** as a man of ordinary prudence would of his own goods (Sec 151); not liable for loss if he took such care (Sec 152).
- Not make **unauthorised use** (Sec 154).
- Not **mix** goods with his own (Sec 155–157).
- **Return** goods on accomplishment of purpose (Sec 160); liable if not returned in time (Sec 161).
- Return any **increase or profit** from the goods (Sec 163) – e.g. calf born to a bailed cow.

Rights of bailee

Right to necessary expenses, compensation, indemnity, and **particular lien** (Sec 170) – right to retain the goods until paid for services involving skill and labour. **General lien** (Sec 171) – bankers, factors, wharfingers, attorneys of

High Court, policy brokers can retain any goods for a general balance.

Finder of goods (Sec 71, 168–169)

A finder is treated as a bailee. He may retain the goods until compensated for expenses; may sue for a specific reward offered; may sell if goods are perishable, owner cannot be found, or lawful charges amount to two-thirds of value.

LEGAL PROVISION Termination of bailment

(1) On the bailee doing any act **inconsistent with the conditions** of bailment – voidable at option of bailor (Sec 153); (2) on **expiry of the period** or **fulfilment of the purpose**; (3) gratuitous bailment – any time by the bailor (Sec 159), or on the **death** of bailor or bailee (Sec 162); (4) destruction of the subject matter.

Rights of bailor against a wrongdoer (Sec 180–181): either the bailor or the bailee may sue a third person who wrongfully deprives the bailee of the goods or injures them; the amount recovered is shared according to their respective interests.

3.4 Pledge (Sec 172)

Pledge (pawn) is the bailment of goods as **security for payment of a debt or performance of a promise**. Bailor = **pawnor/pledgor**; bailee = **pawnee/pledgee**.

Rights of pawnee

- Retain goods for debt, interest and expenses (Sec 173–174).
- Extraordinary expenses (Sec 175).
- On default – sue the pawnor, retain goods as collateral, or **sell after reasonable notice** (Sec 176); shortfall recoverable, surplus to be returned.

Pledge by non-owners

Valid pledge by: mercantile agent in possession with owner's consent (Sec 178), person in possession under voidable contract not yet rescinded (Sec 178A), seller or buyer in possession after sale, co-owner in sole possession, and a person having limited interest (Sec 179).

Bailment vs pledge

Basis	Bailment	Pledge
Purpose	Any purpose (repair, safe custody)	Security for a debt
Use of goods	Bailee may use as agreed	Pawnee cannot use
Right to sell	No (only in specified cases)	Yes, after notice on default
Consideration	May be gratuitous	Always for consideration (the debt)

LEGAL PROVISION Duties of pawnee

Take reasonable care of the goods (Sec 151); not to use the goods; return the goods on payment of the debt; deliver any **accretion** (e.g., bonus shares) to the pawnor; on sale after default, account for any **surplus** to the pawnor (Sec 176).

3.5 Agency (Sec 182–238)

An **agent** is a person employed to do any act for another or to represent another in dealings with third persons. The person represented is the **principal**. The basic rule: *qui facit per alium facit per se* – he who acts through another acts himself.

- Any person of majority and sound mind can appoint an agent; a **minor can be an agent** (but is not personally liable to the principal) (Sec 184).
- No consideration is necessary (Sec 185).

Creation of agency

Mode	Example
Express (oral or written – power of attorney)	Appointing a broker in writing
Implied – by conduct, by estoppel (holding out)	Wife buying household necessaries (agency of necessity of wife)
Agency of necessity	Ship captain selling perishable cargo in emergency
By ratification (Sec 196)	Principal later adopts an act done without authority – must be in existence and competent at the time of act; whole act must be ratified; within reasonable time
By operation of law	Partners are agents of the firm; promoters for the company

Types of agents

General agent, special agent, universal agent, mercantile agents – **factor**, **broker**, **commission agent**, **del credere agent** (guarantees payment by third parties for extra commission), **auctioneer**, **banker**; sub-agent (Sec 191) and substituted agent (Sec 194).

Duties of agent

Follow principal's directions or customs (Sec 211), act with reasonable skill and diligence (Sec 212), render proper accounts (Sec 213), communicate with principal in difficulties (Sec 214), not deal on own account secretly (Sec 215–216), pay sums received (Sec 218), not delegate (*delegatus non potest delegare*), not disclose confidential information.

Rights of agent

Remuneration (Sec 219), retention of sums (Sec 217), **lien** on principal's property (Sec 221), indemnity for lawful acts (Sec 222) and acts done in good faith (Sec 223), compensation for injury caused by principal's neglect (Sec 225).

Termination of agency (Sec 201)

By revocation by principal, renunciation by agent, completion of business, death or insanity of either, insolvency of principal, expiry of time, destruction of subject matter, principal becoming alien enemy. **Irrevocable agency (Sec 202)** – where the agent has an interest in the subject matter (agency coupled with interest).

⚠ COMMON MISTAKE **A minor can be an agent but cannot be a principal (he cannot appoint an agent because he cannot contract).**

⚖ LEGAL PROVISION **Sub-agent vs substituted agent (Sec 191–194)**

A **sub-agent** is employed by and acts under the control of the original agent; no privity with the principal (except fraud/wilful wrong). A **substituted agent** is named by the agent on express/implied authority of the principal and becomes the **principal's own agent**. If A authorises B, who appoints C as substituted agent, and A revokes B's authority, C's authority **continues** – it was derived from A.

Personal liability of agent (Sec 230): an agent cannot personally enforce or be bound by contracts on behalf of the principal, except where (1) he contracts for a **foreign principal** (presumed), (2) the principal is **undisclosed**, (3) the principal **cannot be sued**, (4) he signs/acts personally, (5) **agency coupled with interest**, (6) **breach of warranty of authority**.

3.6 Duties of a bailee and an agent (frequently examined)

LEGAL PROVISION **Bailee – unauthorised use and mixing of goods (s. 151–157)**

s. 151–152: the bailee must take as much care as a man of ordinary prudence would take of his own goods; not liable for loss if he took that care. **s. 153:** the bailment is **voidable** if the bailee acts inconsistently with the conditions. **s. 154:** a bailee who makes **unauthorised use** of the goods is liable to compensate the bailor for **any damage** arising from that use – even if he (or the person he permitted) was careful. **s. 155:** mixing with the bailor's consent – both have an interest in proportion to their shares. **s. 156:** mixing **without consent**, goods **can be separated** – property remains with each party; the **bailee bears the expense of separation** and any damage. **s. 157:** mixing without consent, goods **cannot be separated** – the bailee must **compensate** the bailor for the loss of the goods.

LEGAL PROVISION **Duties of an agent (s. 211–221)**

s. 211: conduct the business according to the principal's **directions**; if he acts otherwise and loss follows, he must **make it good**, and any profit goes to the principal. **s. 212:** act with reasonable **skill and diligence**. **s. 213:** render proper **accounts**. **s. 214:** communicate with the principal in difficulty. **s. 215–216:** not deal on his own account without consent. **s. 217–218:** may retain his remuneration and expenses from sums received, and must pay the balance to the principal. **s. 219:** remuneration becomes due only on **completion** of the act. **s. 220:** an agent guilty of **misconduct** in the business is **not entitled to remuneration** for that part of the business. **s. 221:** lien on the principal's property.

Chapter 4: The Sale of Goods Act, 1930

4.1 Contract of sale (Sec 4)

A **contract of sale of goods** is a contract whereby the seller **transfers or agrees to transfer** the property (ownership) in goods to the buyer for a price. It includes both a **sale** (property passes immediately) and an **agreement to sell** (property passes at a future time or on fulfilment of a condition).

Essentials

Two parties (buyer and seller), **goods** (movable property other than actionable claims and money – includes stock, shares, growing crops, grass), **price** (money consideration – barter is not sale), transfer of general property, and all essentials of a valid contract.

Sale vs agreement to sell

Basis	Sale	Agreement to sell
Transfer of property	Immediate	Future / on condition
Nature	Executed contract	Executory contract
Risk	Passes to buyer (risk follows ownership)	Remains with seller
Remedy on breach by buyer	Suit for price	Suit for damages
Insolvency of buyer	Seller must deliver goods (gets only a dividend in insolvency) unless he has a lien	Seller may refuse to deliver until paid
Resale by seller	Not valid (except for unpaid seller)	Valid – buyer can sue for damages only

Types of goods (Sec 6)

Existing (owned or possessed by seller – specific, ascertained, unascertained), **future** (to be produced or acquired after the contract – only an agreement to sell), and **contingent** goods (acquisition depends on an uncertain event).

LEGAL PROVISION **Sale vs hire-purchase**

Under **hire-purchase**, goods are delivered on payment of instalments as hire charges; the hirer has an **option** to buy on paying the last instalment. Differences: (1) **ownership** passes at once in sale, only on last payment in hire-purchase; (2) buyer is owner vs hirer is a **bailee**; (3) buyer **cannot return** goods vs hirer may return and stop paying; (4) risk of loss after sale on buyer; in hire-purchase the hirer is liable only for negligence; (5) buyer can pass good title to a third party; a hirer cannot; (6) sales tax/GST and price structure differ (hire charges include interest).

4.2 Conditions and warranties (Sec 11–17)

Basis	Condition (Sec 12(2))	Warranty (Sec 12(3))
Meaning	Stipulation **essential** to the main purpose of the contract	Stipulation **collateral** to the main purpose
Breach effect	Buyer can **reject the goods** and treat the contract as repudiated, and claim damages	Buyer can only claim **damages**; cannot reject
Conversion	Breach of condition can be treated as breach of warranty (Sec 13)	Warranty cannot become a condition

Implied conditions

1. **Title (Sec 14(a))** – seller has the right to sell (*Rowland v. Divall*).
2. **Sale by description (Sec 15)** – goods must correspond with the description.
3. **Sale by sample (Sec 17)** – bulk must correspond with sample; buyer has reasonable opportunity to compare; free from hidden defects.
4. **Sample + description** – must correspond with both.

5. **Quality or fitness for purpose (Sec 16(1))** – where buyer makes known the purpose and relies on seller's skill, goods dealt by seller (*Priest v. Last* – hot water bottle).
6. **Merchantable quality (Sec 16(2))** – where goods bought by description from a dealer.
7. **Wholesomeness** – eatables must be fit for human consumption (*Frost v. Aylesbury Dairy* – typhoid milk).

Implied warranties

Quiet possession (Sec 14(b)), freedom from encumbrances (Sec 14(c)), warranty to disclose dangerous nature of goods, and warranty of quality by trade usage (Sec 16(3)).

> ⚖ LEGAL PROVISION **When breach of condition is treated as breach of warranty – Sec 13**
>
> (1) The buyer **waives** the condition; (2) the buyer **elects** to treat it as a warranty; (3) the contract is **non-severable** and the buyer has **accepted** the goods or part of them; (4) the fulfilment is excused by law (impossibility). In these cases the buyer can only claim damages and cannot reject the goods.

4.3 Caveat emptor (Sec 16)

Caveat emptor means "**let the buyer beware**". The buyer must examine the goods and satisfy himself; the seller is not responsible for their quality or fitness unless there is an implied condition.

Exceptions

- Fitness for buyer's purpose made known and reliance on seller's skill.
- Merchantable quality – goods bought by description from a dealer (unless defects are visible on examination).
- Usage of trade.
- Sale by sample, or by description and sample.
- Consent of buyer obtained by **fraud** or active concealment of defects.

> ℹ NOTE **Modern consumer law (Consumer Protection Act, 2019) has shifted the balance towards caveat venditor – "let the seller beware" – through product liability and unfair trade practices.**

4.4 Transfer of property (Sec 18–25)

Property means ownership; **possession** means custody. Rule: **risk passes with property** (Sec 26), whether or not delivery has been made.

Situation	When property passes
Unascertained goods (Sec 18)	Not until goods are ascertained
Specific goods in deliverable state (Sec 20)	When the contract is made – even if payment or delivery is postponed
Specific goods – something to be done to make deliverable (Sec 21)	When it is done and buyer has notice
Specific goods – to be weighed/measured for price (Sec 22)	When done and buyer has notice
Goods on approval / sale or return (Sec 24)	When buyer signifies approval, or retains the goods beyond the time fixed / reasonable time, or does an act adopting the transaction
Unascertained / future goods by description (Sec 23)	When goods are **unconditionally appropriated** to the contract with assent of the other party
Reservation of right of disposal (Sec 25)	When conditions are fulfilled

Transfer of title by non-owners – *nemo dat quod non habet*

"No one can give what he does not have." **Exceptions:** sale by mercantile agent, by one of joint owners, under voidable contract (before rescission), by seller in possession after sale, by buyer in possession, by finder of goods, by pawnee, estoppel.

LEGAL PROVISION **Reservation of right of disposal – Sec 25**

The seller may reserve the right of disposal of goods until certain conditions (usually payment) are fulfilled; property does not pass until then, even if goods are delivered to the buyer or a carrier. The seller is **presumed** to have reserved it where (1) goods are shipped and the **bill of lading** is made out to the order of the seller or his agent; (2) the seller sends the bill of exchange with the bill of lading and the buyer does not honour the bill – the buyer must return the bill of lading, and if he wrongfully retains it, property does not pass.

LEGAL PROVISION **Sale on approval / "sale or return" – Sec 24**

Property passes to the buyer when he (a) signifies approval or does any act **adopting** the transaction (e.g., pledges the goods), or (b) retains the goods beyond the fixed time (or a reasonable time) without giving notice of rejection.

4.5 Performance of the contract – delivery and acceptance (Sec 31–44)

Section	Rule
31–32	Seller must deliver and buyer must accept and pay; delivery and payment are **concurrent conditions** unless otherwise agreed
33	Delivery may be **actual, symbolic** (keys of godown) or **constructive** (attornment by a person in possession)
34	Part delivery in progress of delivery of the whole has the effect of delivery of the whole
35	Seller is not bound to deliver until the buyer **applies** for delivery
36	Place – where goods are at the time of sale; time – reasonable time; expenses of putting goods in deliverable state – seller
37	**Wrong quantity:** less – buyer may reject or accept and pay pro-rata; more – reject all, accept contract quantity and reject the rest, or accept all at contract rate; **mixed** with goods of a different description – accept contract goods and reject the rest, or reject all
38	Buyer is not bound to accept delivery by **instalments** unless agreed
39	Delivery to a carrier is prima facie delivery to the buyer
41–42	Buyer has a reasonable opportunity to examine; acceptance by intimation, by act inconsistent with seller's ownership, or retention beyond reasonable time
43	Buyer is not bound to return rejected goods – notice of refusal is enough
44	Buyer liable for loss and charges if he neglects to take delivery after request

4.6 Unpaid seller (Sec 45–54)

A seller is **unpaid** when the whole price has not been paid or tendered, or a bill of exchange/cheque received as conditional payment has been dishonoured.

Rights against the goods

Right	When available
Lien (Sec 47–49)	Seller in possession: goods sold without credit, credit expired, or buyer insolvent. Lost by delivery to carrier without reservation, buyer's lawful possession, waiver
Stoppage in transit (Sec 50–52)	Seller has parted with possession, goods in transit, and **buyer becomes insolvent**
Resale (Sec 54)	Goods perishable, right of resale reserved, or after notice to buyer who does not pay within reasonable time

Rights against the buyer personally

Suit for price (Sec 55), suit for damages for non-acceptance (Sec 56), suit for repudiation before due date (Sec 60), suit for interest (Sec 61).

Buyer's remedies

Damages for non-delivery (Sec 57), specific performance for specific goods (Sec 58), remedy for breach of warranty (Sec 59), anticipatory breach (Sec 60), interest and special damages (Sec 61).

LEGAL PROVISION Right of resale – Sec 54

The unpaid seller in possession may resell when (1) the goods are of a **perishable** nature; (2) he gives **notice of intention** to resell and the buyer does not pay within a reasonable time; (3) he has **expressly reserved** the right of resale in the contract. In (2) and (3) the seller can recover the loss on resale from the original buyer; if the goods are perishable or notice given, he keeps any profit. The new buyer gets a **good title**.

Specific performance (Sec 58): in a suit for breach of contract to deliver **specific or ascertained** goods, the court may direct delivery without giving the seller the option of paying damages – used where goods are unique (a painting, customised machine).

4.7 Auction sale (Sec 64)

Sale is complete when the auctioneer announces it by the fall of the hammer; bid can be withdrawn before that. Seller may reserve a right to bid (by notification); **pretended bidding** (by seller's agents to raise price) makes the sale voidable at buyer's option.

WORKED EXAMPLE Transfer of property and risk

Ravi buys a specific sofa from a shop on Monday, agreeing to collect it on Wednesday and pay then. The shop catches fire on Tuesday without the seller's fault.

The sofa was specific and in a deliverable state → property passed on Monday (Sec 20) → risk passed with property (Sec 26) → Ravi bears the loss and must pay the price.

Chapter 5: The Negotiable Instruments Act, 1881

A **negotiable instrument** means a promissory note, bill of exchange or cheque payable either to order or to bearer. It is a written document that entitles a person to a sum of money and is transferable by delivery (bearer) or by endorsement and delivery (order).

Characteristics

Freely transferable; holder in due course gets a **good title** even if the transferor's title is defective; holder can sue in his own name; presumptions (Sec 118) – consideration, date, time of acceptance, transfer before maturity, order of endorsements, stamp, holder in due course.

5.1 Promissory note, bill of exchange and cheque

Basis	Promissory note (Sec 4)	Bill of exchange (Sec 5)	Cheque (Sec 6)
Nature	Unconditional **promise** to pay	Unconditional **order** to pay	Bill drawn on a specified **banker**, payable **on demand**
Parties	Two – maker, payee	Three – drawer, drawee, payee	Three – drawer, drawee bank, payee
Acceptance	Not required	Required (except on-demand bills)	Not required
Payable to bearer	Cannot be made payable to bearer	Cannot be made payable to bearer on demand	Can be payable to bearer
Liability of maker/drawer	Primary	Secondary (drawee primary after acceptance)	Primary (if bank dishonours)
Grace days	3 days (time instruments)	3 days (time instruments)	No grace
Crossing	Not possible	Not possible	Possible
Stamp	Required	Required (except on-demand bills)	Not required

A cheque includes an **electronic image of a truncated cheque** and a cheque in electronic form. Cheques are valid for **3 months** from the date of issue (RBI direction).

LEGAL PROVISION Essentials of a valid promissory note

(1) In **writing**; (2) an express **promise** to pay (mere acknowledgment of debt – "I owe you ₹500" – is not a promissory note); (3) promise **unconditional**; (4) **signed** by the maker; (5) maker must be a **certain** person; (6) payee must be **certain**; (7) sum payable must be **certain**; (8) payable in **money** only; (9) not payable to bearer (Sec 31 RBI Act); (10) duly **stamped**.

Additional features of a cheque that distinguish it from a bill: always drawn on a **specified banker**; always payable **on demand**; no acceptance needed; no grace days; may be crossed; no stamp needed; drawer is not discharged by delay in presentment unless he suffers loss.

5.2 Classification by manner of making

Class	Section	Meaning
Inland instrument	11	Drawn or made in India and payable in, or drawn on a person resident in, India
Foreign instrument	12	Any instrument which is not inland
Demand instrument	19, 21	Payable on demand, at sight, on presentment, or where no time is specified
Time instrument	21	Payable after a fixed period, after sight, or on a specified date
Ambiguous instrument	17	Can be construed either as a promissory note or a bill (e.g., drawer and drawee same person) – the **holder may treat it as either**, and once chosen it is treated so thereafter
Inchoate (incomplete) instrument	20	A signed stamped paper delivered blank or incomplete – gives *prima facie* authority to the holder to complete it for any amount up to the stamp's coverage
Bearer / order instrument	13	Payable to bearer (by delivery) or to order (by endorsement + delivery)

5.3 Maturity and days of grace (Sec 21–25)

- Every time instrument is due on the **third day after** the day on which it is expressed to be payable (3 days of grace) – Sec 22. No grace for demand instruments.
- If the maturity date is a **public holiday**, the instrument is due on the **preceding business day** (Sec 25).
- "**Months after date/sight**" – maturity is the corresponding date of the month (or last day of the month) + 3 days (Sec 23). "**Days after date/sight**" – exclude the day of the instrument/presentment (Sec 24).
- A bill payable "after sight" – time runs from the date of **acceptance** or of noting/protest for non-acceptance.

5.4 Parties, holder and holder in due course

- **Holder (Sec 8)** – person entitled in his own name to possession and to recover the amount.
- **Holder in due course (Sec 9)** – a holder who obtained the instrument **for consideration**, **before maturity**, and **in good faith** without notice of defect in title. Privileges: gets title free of defects (Sec 53), every prior party is liable to him until paid (Sec 36), no defence of incomplete instrument (Sec 20), estoppel against denying validity (Sec 120–122).

5.5 Negotiation, endorsement and crossing

- **Negotiation (Sec 14):** transfer so as to make the transferee the holder. Bearer instrument – by **delivery** (Sec 47); order instrument – by **endorsement and delivery** (Sec 48). Delivery is essential – an instrument endorsed but not delivered is not negotiated (Sec 46).
- An instrument **cannot be negotiated** where it is (i) restrictively endorsed ("pay A only"), (ii) drawn with words prohibiting transfer, (iii) already **discharged** by payment at or after maturity (Sec 60), or (iv) crossed "not negotiable" – transferable but transferee gets no better title.

Types of endorsement

Blank/general (only signature), special/full (names endorsee), restrictive ("pay A only"), partial (part amount – invalid as negotiation), conditional ("pay A on arrival of ship"), *sans recours* (without recourse to endorser), facultative (waiver of notice).

Crossing of cheques (Sec 123–131)

Crossing	Form	Effect
General	Two parallel transverse lines, with or without "& Co."	Payable only through a bank account
Special	Name of a banker written across	Payable only through that banker
Restrictive ("Account Payee")	"A/c Payee only"	Collecting bank must credit only the payee's account
Not negotiable	Words "not negotiable" with crossing	Transferable, but transferee gets no better title than transferor

5.6 Presentment and dishonour

Rule	Detail
Presentment for acceptance (Sec 61)	Bills payable after sight must be presented to the drawee for acceptance within a reasonable time
Presentment for payment (Sec 64)	Must be presented for payment, otherwise prior parties are discharged
Presentment unnecessary (Sec 76)	Maker/drawer/acceptor intentionally prevents presentment; place of business closed on due date; no person at the place to pay; cannot be found after due search; party has engaged to pay notwithstanding non-presentment; presentment waived; drawer could not suffer damage from non-presentment
Dishonour by non-acceptance / non-payment (Sec 91–92)	Drawee refuses to accept within 48 hours; or maker/acceptor defaults in payment

Rule	Detail
Notice of dishonour (Sec 93)	Holder must give notice to all prior parties he wants to make liable
Notice unnecessary (Sec 98)	Dispensed with by the party entitled; drawer has countermanded payment; party charged could not suffer damage; party cannot be found; omission due to unavoidable circumstances; acceptor is also the drawer; promissory note is not negotiable; party entitled promises to pay with knowledge of the facts

LEGAL PROVISION Compensation on dishonour – Sec 117

The holder can recover from the drawer/endorser: (a) the **amount due** with **expenses** of presentment, noting and protest; (b) where the person charged resides at a different place from where the instrument was payable – the sum at the **current rate of exchange** between the two places; (c) an endorser who has paid can recover the amount paid with **interest at 18% p.a.** from the date of payment until realisation, plus expenses; (d) re-exchange charges where the bill is drawn on a foreign country.

5.7 Dishonour of cheque – Section 138

Dishonour of a cheque for **insufficiency of funds** (or exceeding arrangement) is a **criminal offence**, if:

1. The cheque was issued for discharge of a **legally enforceable debt or liability**.
2. Presented within **3 months** from date (or its validity period).
3. Payee gives a **written notice** demanding payment within **30 days** of receiving information of dishonour.
4. Drawer fails to pay within **15 days** of receipt of the notice.
5. Complaint filed before a Magistrate within **1 month** after the 15 days expire.

Punishment: imprisonment up to **2 years**, or fine up to **twice the cheque amount**, or both. Court may order **interim compensation up to 20%** of the cheque amount (Sec 143A). Offence is compoundable (Sec 147).

WORKED EXAMPLE Timeline under Sec 138

Cheque dated 1 June, presented 10 July, dishonoured 12 July; payee informed 13 July.

Notice must be sent by 12 August (30 days). Drawer receives notice 16 August → has till 31 August to pay. If not paid, cause of action arises 1 September; complaint by 30 September.

NOTE **Section 138 requires a legally enforceable debt – a cheque issued as a gift or donation does not attract Sec 138 (June 2024 question).**

5.8 Inland, foreign and international instruments (s. 11–12, 134–137)

- **Inland instrument (s. 11):** drawn or made in India and payable in, or drawn on a person resident in, India. **Foreign instrument (s. 12):** any instrument that is not inland.
- **s. 134:** in the absence of a contract to the contrary, the liability of the maker or drawer of a foreign instrument is governed by the **law of the place where it is made**, and that of the acceptor or endorser by the law of the place where the instrument is made **payable**.
- **s. 135:** where an instrument is payable in a different place, the **law of the place of payment** determines what constitutes dishonour and the notice of dishonour.
- **s. 136:** an instrument made outside India is to be interpreted in India by the law of the place where it was made, but a negotiation in India gives the transferee the rights of an Indian holder.
- **s. 137:** the law of a foreign country regarding negotiable instruments is **presumed to be the same as Indian law**, unless proved otherwise.

Chapter 6: The Indian Partnership Act, 1932

6.1 Partnership – definition and nature

Partnership is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all. Persons are individually called **partners** and collectively a **firm**; the name under which business is carried on is the **firm name**.

Essentials

1. **Agreement** – partnership arises from contract, not status (Sec 5) – an HUF business is not a partnership.
2. **Two or more persons** – maximum **50** partners (Companies (Miscellaneous) Rules, 2014 under Sec 464 of Companies Act 2013).
3. **Business** – a lawful business (includes trade, occupation, profession).
4. **Sharing of profits** – sharing of losses is implied but not essential to the definition.
5. **Mutual agency** – the business is carried on by all or any of them acting for all – the **true test** of partnership (*Cox v. Hickman*).

Partnership deed

A written agreement containing name of firm, names of partners, nature and place of business, capital contributions, profit-sharing ratio, interest on capital and drawings, salaries, rules for admission, retirement and dissolution, settlement of accounts. Stamp duty applies. If the deed is silent, the following rules of the Act apply.

Matter	Rule if no agreement
Profit sharing	Equal
Interest on capital	Not allowed (if allowed, only out of profits)
Interest on drawings	Not charged
Interest on loan by partner	**6% p.a.** (Sec 13(d))
Salary/remuneration	Not allowed

LEGAL PROVISION Test of partnership – Sec 6

Sharing of profits is **not conclusive** evidence of partnership. The real test is **mutual agency** – whether the business is carried on by all or by any of them acting for all (*Cox v. Hickman*). Co-owners sharing rent, a joint purchase of goods for resale on a single occasion without an agreement to share profits, or lenders/servants receiving a share of profit are not partners. A husband and wife can be partners if the essentials are present.

6.2 Types of partners

Type	Feature
Active / working partner	Takes part in management
Sleeping / dormant partner	Contributes capital, shares profits, does not take part; liable to third parties
Nominal partner	Lends only name; liable to third parties
Partner by estoppel / holding out (Sec 28)	Represents himself as a partner; liable to those who gave credit on that basis
Partner in profits only	Shares profits but not losses
Minor admitted to benefits (Sec 30)	Shares profits; liability limited to share in firm; within 6 months of majority must elect to become or not become partner (public notice)
Sub-partner	Shares his own share with an outsider; not a partner of the firm

LEGAL PROVISION **Minor admitted to the benefits of partnership – Sec 30**

A minor cannot be a partner, but may be **admitted to the benefits** with the consent of all partners.

Rights: share of property and profits as agreed; access to and copy of accounts (not books); sue for his share when severing connection; within **6 months** of attaining majority (or of knowing of his admission, whichever is later) elect by **public notice** to become or not to become a partner.

Liabilities (before majority): his **share** in the property and profits is liable for the acts of the firm; he is **not personally liable**. If he becomes a partner on majority he is personally liable for all acts from the date of his admission to benefits; if he elects not to, he is not liable for acts after the notice.

6.3 Rights, duties and liabilities of partners

- **Rights (Sec 12–13):** take part in business, be consulted, access books, share profits equally, interest on capital/advances, indemnity, prevent admission of new partner without consent, retire.
- **Duties (Sec 9–16):** carry on business to greatest common advantage, be just and faithful, render true accounts, indemnify for fraud and wilful neglect, not compete, account for personal profits.
- **Liability (Sec 25):** every partner is **jointly and severally liable**, without limit, for all acts of the firm done while he is a partner.
- **Implied authority (Sec 19):** a partner can bind the firm for acts done in the usual way of business; he **cannot** (without express authority) submit to arbitration, open a bank account in his own name, compromise a claim, withdraw a suit, admit liability in a suit, acquire or transfer immovable property, or enter into partnership on behalf of the firm.

LEGAL PROVISION **Mutual rights (Sec 12–13) and implied authority (Sec 19)**

Unless agreed otherwise: every partner may take part in business; differences decided by **majority** but change in nature of business needs **consent of all**; every partner may inspect and copy books; **no remuneration**; profits and losses shared **equally**; **no interest on capital** (if agreed, payable only out of profits); **interest on advances at 6% p.a.**; firm must **indemnify** a partner for payments made in the ordinary course or in an emergency; a partner must indemnify the firm for loss caused by his **wilful neglect**.

No implied authority (Sec 19(2)) to: submit a dispute to arbitration; open a bank account in his own name; compromise or relinquish a claim; withdraw a suit; admit liability in a suit; acquire or transfer **immovable property** of the firm; enter into partnership on behalf of the firm.

Holding out (Sec 28): a person who represents himself, or knowingly permits himself to be represented, as a partner is liable to those who gave credit on that faith. Exception: after a partner's death, the use of the old firm name does not make his estate liable.

Transfer of interest (Sec 29): a partner can transfer his share **without consent** only in the sense of assigning his right to profits; the transferee **cannot interfere** in business or inspect books; he may receive the share of profits and accept the account agreed by partners. On dissolution he gets the transferor's share of assets and may ask for an account from the date of dissolution.

6.4 Reconstitution of a firm (Sec 31–38)

Event	Rules
Introduction of a partner (Sec 31)	Needs **consent of all** existing partners; incoming partner not liable for acts done before he became a partner (unless he agrees)
Retirement (Sec 32)	With consent of all, as per agreement, or by notice in a partnership at will. Retiring partner remains liable to third parties for acts before retirement; and for acts after retirement until **public notice** is given
Expulsion (Sec 33)	Valid only if (1) the **power** is conferred by contract, (2) exercised by a **majority** of partners, (3) in **good faith** (notice and opportunity to be heard). Otherwise null and void. An expelled partner is not liable for acts after expulsion once public notice is given
Insolvency (Sec 34)	Insolvent partner ceases to be a partner from the date of adjudication; his estate not liable for later acts

Event	Rules
Death (Sec 35)	Estate of a deceased partner not liable for acts after death
Outgoing partner – competing business (Sec 36)	May carry on a competing business and advertise it, but may **not** use the firm name, represent himself as carrying on the firm's business, or solicit the firm's old customers. A **restraint agreement** (not to carry on similar business within specified period/local limits) is valid if reasonable
Share of subsequent profits (Sec 37)	If the continuing partners carry on business without settling accounts, the outgoing partner (or his estate) may claim at his option profits attributable to the use of his share **or interest at 6% p.a.** on it

6.5 Registration of firms (Sec 58–59, 69)

Registration is **optional** (not compulsory) but has important consequences. Application in the prescribed form to the Registrar of Firms with firm name, place of business, other places, date of joining of each partner, names and addresses, and duration.

Effects of non-registration (Sec 69)

- A partner cannot sue the firm or other partners.
- The firm cannot sue third parties for enforcing a contract.
- The firm cannot claim set-off above ₹100.
- But: third parties **can** sue the firm; partner can sue for dissolution and accounts; suits up to ₹100 and in areas exempt are allowed.

LEGAL PROVISION Cases where non-registration does not affect rights (Sec 69(3)–(4))

A partner of an unregistered firm may sue for **dissolution**, for **accounts** of a dissolved firm or for realising the property of a dissolved firm; the Official Assignee may realise property of an insolvent partner; the firm may sue/claim set-off for an amount **not exceeding ₹100**; suits arising otherwise than out of contract; firms with no place of business in the territories to which the Act applies; and **third parties** can always sue the unregistered firm. Non-registration bars: a partner suing the firm or co-partners, and the firm suing third parties or claiming a **set-off** exceeding ₹100.

6.6 Dissolution of firm (Sec 39–55)

Mode	Section
By agreement	40
Compulsory – all or all but one partner insolvent; business becomes unlawful	41
On happening of contingencies – expiry of term, completion of venture, death, insolvency of a partner (subject to contract)	42
By notice – partnership at will	43
By court – insanity, permanent incapacity, misconduct, wilful breach, transfer of interest, perpetual losses, just and equitable	44

Settlement of accounts (Sec 48): losses (including capital deficiencies) paid first from profits, then capital, then partners individually in profit ratio. Assets applied: (i) third-party debts, (ii) partners' advances, (iii) partners' capital, (iv) residue in profit ratio. *Garner v. Murray* rule – solvent partners bear the insolvent partner's capital deficiency in the ratio of their capitals.

LEGAL PROVISION **After dissolution (Sec 45–48)**

Sec 45 – partners remain liable for acts done after dissolution until **public notice** is given. **Sec 46** – every partner (or his representative) may have the business **wound up** and property applied in payment of debts and the surplus distributed. **Sec 47** – authority of each partner continues so far as necessary to **wind up** the affairs and complete transactions begun but unfinished. **Sec 48 – mode of settlement:** (a) losses (including capital deficiency) paid first out of profits, then out of capital, then by partners individually in profit-sharing ratio; (b) assets applied in order: (i) debts to **third parties**; (ii) **advances** of partners; (iii) **capital** of partners; (iv) surplus in profit-sharing ratio.

Dissolution of partnership vs dissolution of firm: dissolution of *partnership* is a change in the relation between partners (retirement, death, admission) – the firm continues; dissolution of the *firm* ends the relation among **all** partners and the business is wound up.

Chapter 7: The Limited Liability Partnership Act, 2008

7.1 Nature and incorporation

- **LLP** is a **body corporate** with **separate legal entity** and **perpetual succession**; partners' liability limited to agreed contribution (except for wrongful acts/fraud). The Partnership Act, 1932 does **not** apply.
- **Minimum 2 partners** (no maximum). If partners fall below 2 and the LLP carries on business for more than **6 months**, the remaining partner who knows of it is **personally liable** for obligations during that period (s. 6).
- **Designated partners (s. 7):** at least **two designated partners who are individuals**, of whom **at least one is resident in India** (stayed in India for at least **120 days** during the financial year VERIFY); where a body corporate is a partner, its nominee individual may act. **DPIN/DIN** required; consent in Form 9 filed with ROC within **30 days** of appointment; vacancy filled within **30 days**. Designated partners are liable for compliance and penalties.
- **Incorporation (s. 11–12):** incorporation document (FiLLiP) with name, business, registered office, names/addresses of partners and designated partners, statement of compliance by an advocate/CA/CS/CMA or a designated partner; certificate of incorporation within 14 days VERIFY.
- **Name (s. 15):** ending with "Limited Liability Partnership" or "LLP"; not undesirable or identical.
- **LLP agreement (s. 23):** mutual rights and duties; filed in **Form 3** within **30 days** of incorporation; changes filed within 30 days. **If no agreement or a matter not covered, First Schedule applies** (e.g. equal share in capital and profits; indemnity by LLP; every partner may take part in management; no remuneration; decisions by majority; change in business only with consent of all partners; partner to account for profits from competing business; expulsion only if power conferred in agreement).

7.2 Partners and their relations

- **s. 24 cessation:** in accordance with agreement, or by **30 days' notice** to other partners (if no agreement); on death, dissolution, insolvency, unsound mind. A former partner is regarded as a partner by third parties **unless** the third party had notice or notice was delivered to the Registrar. Cessation does not discharge his liability for obligations incurred **while he was a partner**. Personal representatives can receive his share of capital and accumulated profits.
- **s. 25 registration of changes:** partner to intimate change in his name/address to the LLP within **15 days**; LLP files notice with ROC within **30 days** of change in partners (Form 4).
- **s. 26 partner as agent:** every partner is an agent of the LLP but **not of other partners**.
- **s. 27 extent of liability of LLP:** LLP is not bound by anything done by a partner without authority when the person dealing knows of it/does not know or believe him to be a partner; LLP **liable for wrongful acts or omissions of a partner** in the course of business or with its authority; obligations of the LLP, in contract or otherwise, are solely its obligations, met out of its property.
- **s. 28:** a partner is **not personally liable** for obligations of the LLP solely by being a partner; **but is personally liable for his own wrongful act or omission** (not for another partner's).
- **s. 29 holding out:** person who represents himself or knowingly permits himself to be represented as a partner is liable to anyone who gave credit on that basis.
- **s. 30 unlimited liability in case of fraud:** acts carried out with intent to defraud creditors – liability of the LLP and the partners who acted is **unlimited** for all debts; fine and imprisonment up to **5 years** for persons knowingly party.
- **Who can be a partner (s. 5):** any **individual** or **body corporate** – but a body corporate excludes a **co-operative society**, a corporation sole and other notified bodies (s. 2(1)(d)); an individual of unsound mind, an undischarged insolvent or one who has applied to be adjudged insolvent cannot be a partner.
- **s. 32 contribution:** tangible, movable or immovable, intangible property, money, promissory notes, other binding agreements to contribute cash or property, and **contracts for services performed or to be performed** (so future services count as contribution); monetary value disclosed. **s. 33** – obligation to contribute is enforceable; creditor may enforce.
- **s. 42 rights of partner to share of profits (transfer):** right to share of profits and losses and to receive distributions is **transferable** wholly or in part; transfer **does not by itself cause disassociation** or dissolution; transferee does **not** get the right to participate in management or access information.

7.3 Accounts, audit, returns

- **s. 34:** proper books on cash or accrual basis and double entry, kept at registered office for **8 years**. **Statement of Account and Solvency (Form 8)** within **30 days from the end of 6 months** of the FY (i.e. by **30 October**). Accounts **audited**, except LLPs with **turnover ≤ ₹40 lakh** or **contribution ≤ ₹25 lakh** in a FY (unless the partners decide to have audit).
- **s. 34A:** Central Government may prescribe accounting standards/auditing standards for classes of LLPs.
- **s. 35 annual return (Form 11)** within **60 days** of the closure of the FY (by 30 May).
- **Small LLP (s. 2(1)(ta)):** contribution ≤ **₹5 crore** (upper prescribed limit) and turnover ≤ **₹50 crore** – lesser penalties VERIFY.
- **Penalties:** after the 2021 amendments, many offences are **civil penalties** adjudicated by the Registrar; compounding under s. 39.

7.4 Conversion, compromise, winding up

- **Conversion into LLP:** firm (**s. 55, Second Schedule**), **private company (s. 56, Third Schedule)** and **unlisted public company (s. 57, Fourth Schedule)** – for companies: no security interest subsisting or all secured creditors consent, all shareholders become partners and no one else; application with statement of shareholders/partners and incorporation document.
- **s. 58 effect of conversion:** the firm/company is **deemed dissolved** and removed from records; **all property, assets, interests, rights, privileges, liabilities and obligations** transfer to and vest in the LLP without further assurance; **pending proceedings** continue by or against the LLP; agreements, contracts, deeds continue as if the LLP were party; **existing employees** continue on the same terms; approvals, permits, licences continue subject to the relevant law. Within **15 days** of registration the LLP informs the concerned Registrar of Firms/ROC. For **12 months** after conversion the LLP states on its correspondence that it was converted from the firm/company VERIFY.
- **s. 60–62 compromise or arrangement:** application to the **Tribunal**; Tribunal may order a meeting; approved by majority representing **three-fourths in value** of creditors/partners present and voting; sanctioned by the Tribunal; order filed with ROC within **30 days**.
- **Winding up (s. 63–65):** voluntary or by the **Tribunal** – grounds: LLP decides to be wound up; partners fall below 2 for more than 6 months; LLP unable to pay its debts; acted against sovereignty/security/public order; default in filing Form 8/Form 11 for 5 consecutive FYs; just and equitable.
- **Foreign LLP (s. 59)**; **whistle-blowing (s. 31)** – Tribunal may reduce penalty of a partner/employee who provides useful information.

7.5 Points frequently examined

- **Conversion of a private company into an LLP (s. 56, Third Schedule):** possible only if (a) there is **no security interest** subsisting or in force on its assets, and (b) **all shareholders become partners** and no one else. The company files an application with the statement of shareholders' consent and incorporation documents; on registration the Registrar issues a certificate, the company is **deemed dissolved**, and its assets, liabilities, rights and obligations **vest in the LLP**. The LLP must state for 12 months in its correspondence that it was converted from the named company VERIFY.
- **Designated partner vacancy (s. 9):** an LLP must appoint a designated partner within **30 days** of a vacancy.
- **Unlimited liability (s. 30):** where any act is carried out with **intent to defraud creditors** or for a fraudulent purpose, the liability of the LLP and the partners concerned is **unlimited**.
- **Auditor (Rule 24 of LLP Rules):** accounts must be audited unless turnover ≤ ₹40 lakh and contribution ≤ ₹25 lakh; the **designated partners** appoint the auditor – the first auditor before the end of the first financial year, later auditors at least 30 days before the end of each financial year; the auditor holds office until the conclusion of the next appointment process VERIFY.

Chapter 8: Industrial Laws – Factories, Gratuity, EPF, ESI and the Code on Wages

8.1 The Factories Act, 1948

Factory – s. 2(m): premises where **10 or more workers** work with the aid of power, or **20 or more** without power, on any day of the preceding 12 months, and a manufacturing process is carried on. **Occupier** – s. 2(n): the person with ultimate control over the affairs of the factory (for a company, any one director). **Worker** – s. 2(l): a person employed directly or through an agency in a manufacturing process or connected work.

Area	Key provisions
Health (s. 11–20)	Cleanliness (11), disposal of wastes (12), ventilation and temperature (13), dust and fume (14), artificial humidification (15), **overcrowding** (16), lighting (17), drinking water (18 – cool water where more than 250 workers), latrines and urinals (19), spittoons (20)
Safety (s. 21–41)	Fencing of machinery (21), work on or near machinery in motion (22), young persons on dangerous machines (23), hoists and lifts (28), pressure plant (31), floors and stairs (32), eye protection (35), dangerous fumes (36), fire precautions (38); **safety officer** where 1,000 or more workers (40B)
Welfare (s. 42–50)	Washing facilities (42); first-aid box – one per **150** workers; **ambulance room** – more than **500** workers (45); **canteen** – more than **250** workers (46); shelters, rest and lunch rooms – more than **150** workers (47); **creche** – more than **30 women** workers (48); **welfare officer** – **500** or more workers (49)
Working hours of adults (s. 51–66)	Weekly hours ≤ **48** (51); weekly holiday (52); daily hours ≤ **9** (54); interval of at least **½ hour** so that no period of work exceeds **5 hours** (55); **spread-over ≤ 10½ hours** (56); **overtime** at **twice** the ordinary rate of wages (59); women normally only between **6 am and 7 pm** (66)
Young persons (s. 67–77)	No child who has not completed **14 years** may work in any factory (67); a child (14–15 years) may work only with a certificate of fitness and not more than **4½ hours** a day, and not at night
Annual leave with wages (s. 79)	A worker who has worked **240 days or more** in a calendar year gets leave of **1 day for every 20 days** worked (child: 1 day for every 15 days)

LEGAL PROVISION Powers of an Inspector (s. 9)

Within the local limits for which he is appointed, an Inspector may: (a) **enter** any place used or intended to be used as a factory, with assistants; (b) **examine** the premises, plant, machinery and any article; (c) **inquire** into any accident or dangerous occurrence; (d) **require production** of registers and documents; (e) **seize or take copies** of registers and records; (f) take **samples** and statements of persons; (g) direct that premises be left undisturbed for examination; (h) take measurements, photographs and recordings; and (i) exercise other powers that may be prescribed. No person can be compelled to answer a question that may incriminate him.

8.2 The Payment of Gratuity Act, 1972

- **Applies** to every factory, mine, oilfield, plantation, port, railway company, shop or establishment employing **10 or more employees** on any day of the preceding 12 months. Once applicable, it continues to apply even if the number falls below 10.
- **Eligibility** (s. 4(1)): gratuity is payable on termination after **at least 5 years of continuous service** – on (a) superannuation, (b) retirement or resignation, or (c) **death or disablement** due to accident or disease. The 5-year condition **does not apply** to death or disablement; on death it is paid to the nominee or heirs.
- **Amount** (s. 4(2)): **15 days' wages for every completed year** of service (or part exceeding **6 months**), at the rate last drawn. For monthly-rated employees: **last monthly wages × 15 ÷ 26 × completed years**. For **seasonal** establishments: **7 days' wages** for each season. Wages = basic + dearness allowance.
- **Ceiling** (s. 4(3)): **₹20,00,000** VERIFY.
- **Forfeiture** (s. 4(6)): to the extent of damage caused by wilful omission or negligence; **wholly or partially** for riotous or disorderly conduct, or an offence involving **moral turpitude** committed in the course of employment.
- **Application and payment** (s. 7 and Rules): the employee applies within **30 days** of gratuity becoming payable; a **belated application** must be accepted if there is sufficient cause for delay. The employer must determine the

amount and **pay within 30 days** of it becoming payable; delay attracts simple **interest**. Disputes go to the **Controlling Authority**.

WORKED EXAMPLE Gratuity

Mr. Rao retires after **24 years and 7 months** of service; last drawn basic + DA ₹52,000 per month. Completed years = **25** (part exceeds 6 months). Gratuity = 52,000 × 15 ÷ 26 × 25 = **₹7,50,000** – within the ₹20 lakh ceiling.

8.3 The Employees' Provident Funds and Miscellaneous Provisions Act, 1952

- **Applies** to every factory in a Schedule I industry and other notified establishments employing **20 or more persons**; may be applied voluntarily with fewer employees.
- **Schemes**: Employees' Provident Fund Scheme 1952, Employees' Pension Scheme 1995 (EPS), Employees' Deposit Linked Insurance Scheme 1976 (EDLI).
- **Contribution**: employee **12%** and employer **12%** of basic wages + DA + retaining allowance (**10%** for notified establishments, sick units, or fewer than 20 employees). Of the employer's share, **8.33%** goes to the EPS (on wages up to **₹15,000** p.m.) and the balance to the PF. Membership is compulsory for employees drawing up to **₹15,000** p.m. VERIFY
- **Withdrawal**: allowed for purposes such as housing (purchase or construction of a dwelling house), marriage, education, illness, and repayment of housing loans, subject to conditions; full settlement on retirement or unemployment for the prescribed period.
- Administered by the **Central Board of Trustees** and the **EPFO**; the employer must deduct and deposit by the **15th** of the following month.

8.4 The Employees' State Insurance Act, 1948

- **Applies** to factories and notified establishments employing **10 or more persons**; covers employees with wages up to **₹21,000** p.m. (₹25,000 for persons with disability) VERIFY.
- **Contribution**: employer **3.25%**, employee **0.75%** of wages; employees earning up to ₹176 a day as average daily wage are exempt from their share VERIFY.
- **Benefits** (s. 46): (1) **sickness** benefit, (2) **maternity** benefit, (3) **disablement** benefit (temporary and permanent), (4) **dependants'** benefit (on death from employment injury), (5) **medical** benefit, and (6) **funeral** expenses; plus unemployment allowance under notified schemes.
- Administered by the **ESI Corporation** and its Standing Committee and Medical Benefit Council; disputes go to the **Employees' Insurance Court**.

8.5 The Code on Wages, 2019

The Code consolidates four Acts: the **Payment of Wages Act, 1936**, **Minimum Wages Act, 1948**, **Payment of Bonus Act, 1965** and **Equal Remuneration Act, 1976**.

Topic	Key provisions
Wages (s. 2(y))	Basic pay + DA + retaining allowance. Specified exclusions (HRA, conveyance, overtime, commission, bonus, etc.); if the excluded items exceed **50%** of total remuneration, the excess is added back to wages
Equal remuneration	No discrimination on the ground of **gender** in wages or recruitment for the same or similar work
Minimum wages	Fixed by the appropriate Government, considering skill, arduousness and geographical area; reviewed at intervals of not more than **5 years**
Floor wage	Fixed by the **Central Government**; minimum wages cannot be below it
Time of payment (s. 17)	Daily – at the end of the shift; weekly – last working day of the week; fortnightly – before the end of the **2nd day** after the fortnight; monthly – before the **7th day** of the next month
Deductions	Only authorised deductions; total deductions not to exceed **50%** of wages
Bonus	Minimum **8.33%** of wages or ₹100, whichever is higher; maximum **20%**; employee must have worked **30 days** in the year; wage threshold to be notified VERIFY

Topic	Key provisions
Overtime	At least **twice** the normal rate of wages
Inspector-cum-facilitator	Replaces the Inspector – advises employers and workers and inspects

COMMON MISTAKE **Common errors in industrial-law answers**

Mixing up thresholds: Factories Act **10/20 workers**, Gratuity **10 employees**, EPF **20 persons**, ESI **10 persons**. Gratuity uses **15/26** for monthly-rated employees, not 15/30.

8.6 Points frequently examined

- **Fines (s. 19, Code on Wages):** only for acts and omissions **specified by the employer** with prior approval of the appropriate Government and notified to employees; only after giving the employee an **opportunity of showing cause**; total fine in a wage period not more than **3% of wages**; **no fine on a person below 15 years**; not recovered by instalments or after **90 days** of the act; recorded in a register and used only for employees' **welfare** VERIFY.
- **Claims (s. 45, Code on Wages):** claims for unpaid wages, bonus or less payment are heard by the **Authority** appointed by the appropriate Government; filed within **3 years** of the date of claim VERIFY.
- **Nomination (Gratuity, Rule 6):** every employee who has completed **one year** of service must nominate one or more persons (in **Form F**) within **30 days**; if he has a family, the nomination must be in favour of **family members** only; a nomination made when he had no family becomes invalid on acquiring a family; it can be changed by written notice.
- **EPF withdrawals and advances:** purchase or construction of a house, repayment of housing loan, marriage of self/children/siblings, post-matric education of children, illness, natural calamity, lock-out or closure, and purchase of equipment by a physically handicapped member; full withdrawal on retirement or after the prescribed period of unemployment VERIFY.

Chapter 9: Companies Act – Preliminary and Kinds of Companies

9.1 Kinds of companies

Type	Key features
Private company – s. 2(68)	Articles restrict transfer of shares; members ≤ **200** (excluding present and former employee-members; joint holders count as one); prohibits invitation to the public to subscribe to securities
Public company – s. 2(71)	Not a private company; a **subsidiary of a public company is deemed public** even if its articles are private
One Person Company (OPC) – s. 2(62)	Only one member – a **natural person who is an Indian citizen** (resident or not) VERIFY; must nominate another such person; cannot be a section 8 company, cannot carry on NBFC investment activities; may convert into private/public company at any time
Small company – s. 2(85)	Private company with paid-up capital ≤ **₹10 crore** and turnover ≤ **₹100 crore** (last year). Not applicable to holding/subsidiary companies, section 8 companies or companies governed by a special Act
Section 8 company	Promotes commerce, art, science, sports, education, research, social welfare, religion, charity, environment etc.; applies profits to objects; **no dividend**; licence from Central Government
Holding / subsidiary – s. 2(46), 2(87)	Holding company **controls the composition of the Board** or exercises/controls **more than one-half of total voting power** (alone or with subsidiaries). Prescribed classes of holding companies cannot have more than **two layers** of subsidiaries
Associate company – s. 2(6)	Company in which another has **significant influence** (control of ≥ **20% of total voting power** or of business decisions under an agreement), but which is not a subsidiary; includes a joint venture
Government company – s. 2(45)	≥ **51% of paid-up share capital** held by Central Government and/or State Governments (includes subsidiary of a Government company)
Listed company – s. 2(52)	Any of its securities listed on a recognised stock exchange (certain classes excluded by rules)
Foreign company – s. 2(42)	Incorporated outside India and having a place of business in India (itself or through an agent, physically or electronically) and conducting business activity in India
Dormant company – s. 455	Formed for a future project or to hold an asset/IPR with no significant accounting transaction; status via MSC-1

9.2 Other important definitions

- **Key Managerial Personnel (KMP)** – s. 2(51): CEO/MD/manager; company secretary; whole-time director; CFO; such other officer, not more than one level below the directors, in whole-time employment, designated as KMP by the Board; any other prescribed officer.
- **Officer who is in default** – s. 2(60): whole-time directors, KMP, directors aware of the contravention (through Board proceedings or without objection), share transfer agents etc.
- **Related party** – s. 2(76): directors, KMP and their relatives; firms in which a director/manager or relative is a partner; private companies in which a director/manager is a member or director; public companies in which a director/manager is a director and holds > 2% of paid-up capital with relatives; holding, subsidiary, associate and fellow subsidiaries.
- **Relative** – s. 2(77): members of a HUF, husband/wife, and prescribed relations (father incl. step-father, mother incl. step-mother, son incl. step-son, son's wife, daughter, daughter's husband, brother incl. step-brother, sister incl. step-sister).
- **Free reserves** – s. 2(43): reserves available for distribution as dividend; **excludes** unrealised gains, notional gains, revaluation reserve and changes in carrying amounts on fair valuation.
- **Net worth** – s. 2(57): paid-up capital + all reserves created out of profits + **securities premium** + debit/credit balance of P&L, less accumulated losses, deferred expenditure and miscellaneous expenditure not written off; excludes revaluation reserves, write-back of depreciation and amalgamation reserves.
- **Turnover** – s. 2(91): gross amount of revenue recognised in P&L from sale, supply or distribution of goods or services during a financial year.

- **Financial year** – s. 2(41): 1 April – 31 March; a company incorporated on or after 1 January may close its first FY on 31 March of the **following** year. A company that is a holding/subsidiary/associate of a company incorporated outside India requiring consolidation abroad may apply to the **Tribunal** for a different FY.

Chapter 10: Companies Act – Incorporation and Matters Incidental Thereto

10.1 Incorporation – sections 3 to 7

- **Formation (s. 3):** public company – 7 or more persons; private company – 2 or more; OPC – 1 person; for any lawful purpose, by subscribing to the memorandum and complying with registration.
- **Memorandum (s. 4):** clauses – **name** (ending with "Limited"/"Private Limited"/"(OPC) Private Limited"), **registered office State**, **objects**, **liability**, **capital** (for companies with share capital), **subscription/association** clause; OPC – nominee. **Reservation of name** via RUN/SPICe+ – valid **20 days** (60 days for proposed name change of existing company) VERIFY.
- **Articles (s. 5):** regulations for management; may contain **entrenchment** provisions (specified provisions altered only if more restrictive conditions are met) – private company: all members' agreement; public company: special resolution; notice to ROC.
- **Incorporation documents (s. 7):** memorandum and articles signed by subscribers; declaration by a professional (CA/CS/CMA/advocate) engaged in formation and by a person named as director/manager/secretary; affidavits of subscribers and first directors; address for correspondence; particulars of subscribers and first directors with DIN; interests in other firms/companies. ROC issues certificate of incorporation with **CIN**.
- **Furnishing false information (s. 7(6)–(7)):** liability for fraud under s. 447; on proof that the company was incorporated by furnishing false information, the **Tribunal** may pass orders including regulating management, removing the name from the register, or winding up; members' liability may be made unlimited.
- **Effect of registration (s. 9):** body corporate with perpetual succession, capacity to hold property, sue and be sued.
- **Effect of memorandum and articles (s. 10):** bind the company and members as if signed by each member; money payable by a member is a debt.
- **Commencement of business (s. 10A):** a company with share capital must file a declaration (INC-20A) within **180 days** of incorporation that every subscriber has paid the value of shares agreed; otherwise penalty (company ₹50,000; officer ₹1,000 per day up to ₹1 lakh) and ROC may strike off.
- **Registered office (s. 12):** within **30 days** of incorporation and at all times; change of office outside the local limits of a city – special resolution; change of State – Central Government (Regional Director) approval and alteration of memorandum. Name, address, CIN, phone, e-mail, website painted/affixed outside every office in **legible letters**, in English and in the local language.

10.2 Alteration of memorandum and articles (s. 13, 14)

Alteration	Requirement
Name	Special resolution + **Central Government** approval (except mere addition/deletion of "Private"); new certificate of incorporation
Registered office from one State to another	Special resolution + **Central Government** approval (application in INC-23); filing within 30 days of order
Objects clause	Special resolution; a company that raised money from the public through a prospectus and has unutilised money – special resolution by **postal ballot**, details in newspapers, dissenting shareholders given an exit opportunity
Liability clause	Special resolution
Capital clause	Section 61 – ordinary resolution
Articles (s. 14)	**Special resolution**; conversion of private into public or vice versa – alteration of articles; public → private requires **Tribunal** approval VERIFY; file with ROC within 15 days

10.3 Doctrines

- **Ultra vires:** an act beyond the objects of the memorandum is void and cannot be ratified even by all members (*Ashbury Railway Carriage v. Riche*).

- **Constructive notice:** every person dealing with a company is deemed to have notice of its public documents (memorandum, articles). (Section 399 allows inspection; the doctrine is regarded as diluted for documents filed electronically VERIFY.)
- **Indoor management (*Royal British Bank v. Turquand*):** outsiders dealing in good faith need not enquire into internal irregularities. **Exceptions:** knowledge of irregularity; suspicion of irregularity/negligence; forgery; act outside the company's or officer's authority; reliance on articles not read.
- **Lifting the corporate veil:** courts disregard separate personality for fraud or improper conduct, tax evasion, a company formed to avoid a legal obligation, enemy character, sham companies, and statutorily under ss. 7(7), 34–36, 339 etc. (*Salomon v. Salomon* – separate entity; *Gilford Motor v. Horne* – veil lifted).

Chapter 11: Companies Act – Prospectus and Allotment of Securities

11.1 Public offer and prospectus

Prospectus (s. 2(70)) – any document described or issued as a prospectus, including a red herring prospectus, shelf prospectus, or any notice, circular, advertisement inviting offers from the public for the subscription or purchase of securities. **Public offer** = initial public offer, further public offer, or **offer for sale** by existing shareholders (s. 23).

Type	Key rules
Shelf prospectus (s. 31)	For prescribed classes (banks, PFIs, etc. as per SEBI); validity **one year** from the opening of the first offer; **information memorandum** with material changes filed before each subsequent offer
Red herring prospectus (s. 32)	Does not contain complete particulars of quantum or price; filed with ROC at least **3 days** before opening of the offer; variations highlighted; prospectus filed after closure with full details
Abridged prospectus (s. 33)	Memorandum containing salient features; must accompany every application form
Deemed prospectus (s. 25)	Securities allotted with a view to offer for sale to the public – document of offer for sale is deemed a prospectus; presumed if offer is made within **6 months** of allotment or before the company receives the whole consideration

Liability for misstatements: s. 34 – criminal (every person who authorises the issue – fraud under s. 447) – defence: statement immaterial or the person believed it true; **s. 35 – civil** (compensation to persons who subscribed relying on it – directors, promoters, experts, those named as directors) – defences: withdrew consent before issue, issued without knowledge/consent and gave public notice on becoming aware; **s. 36 – fraudulently inducing** persons to invest money – punishable under s. 447.

11.2 Allotment (s. 39, 40)

- **Minimum subscription** stated in the prospectus must be received and the **application money ≥ 5%** of the nominal amount of the security (or as SEBI specifies) must be paid before allotment.
- If minimum subscription is not received within **30 days** from the date of issue of the prospectus (or as SEBI specifies), the money must be **repaid within 15 days** after that (SEBI specifies timelines for listed issues).
- **Return of allotment** in PAS-3 within **30 days** of allotment.
- **Listing (s. 40):** application to one or more recognised stock exchanges before the public offer; money kept in a separate bank account and used only for adjustment against allotment or repayment.

11.3 Private placement (s. 42 and Rule 14)

- Offer to **identified persons** through a private placement offer-cum-application letter (**PAS-4**), with a record of offers (PAS-5); approved by **special resolution** for each offer (a single special resolution for a year allowed for non-convertible debentures).
- Offer/invitation to not more than **200 persons in aggregate in a financial year** (excluding **qualified institutional buyers** and employees under ESOP), counted separately for each kind of security.
- **Minimum value of offer per person ₹20,000** of face value of securities.
- Application money only by **cheque/demand draft/banking channel**, not cash; kept in a separate bank account.
- **Allotment within 60 days** of receiving application money, else refund within **15 days** thereafter; beyond that, interest **@ 12% p.a.** from the 60th day.
- **Return of allotment** (PAS-3) within **15 days** of allotment. No fresh offer until the earlier allotments are completed, withdrawn or abandoned. Companies cannot release public advertisements or use intermediaries to inform the public.
- An offer to more than the permitted number of persons is deemed a **public offer** (prospectus rules apply).

Chapter 12: Companies Act – Share Capital and Debentures

12.1 Kinds of share capital and key sections

- **s. 43:** equity share capital (with voting rights, or with **differential rights** as to dividend, voting or otherwise as per rules) and **preference** share capital (preferential right to dividend and to repayment of capital on winding up).
- Equity shares with **differential rights** (Rule 4): authorised by articles and ordinary resolution (postal ballot for listed); **shares with differential rights ≤ 74%** of total post-issue paid-up equity capital including such shares; track record of **distributable profits for three years**; no default in filing financial statements/annual returns for 3 years, in repayment of deposits/debentures/loans, in dividend payment VERIFY.
- **s. 47 voting rights:** equity holder votes in proportion to paid-up equity share capital; preference shareholders vote only on resolutions directly affecting their rights, on winding up, repayment/reduction of capital, and on every resolution if dividend is unpaid for **two years or more**.
- **s. 48 variation of shareholders' rights:** with **written consent of holders of ≥ ¾ of the issued shares of that class** or a **special resolution at a separate meeting** of that class (and if provided in memorandum/articles, or not prohibited by the terms of issue). Holders of ≥ **10% of issued shares** of that class who did not consent may apply to the **Tribunal within 21 days** to have the variation cancelled; the variation then has effect only if confirmed by the Tribunal.
- **s. 52 securities premium** – may be applied only for: issue of **fully paid bonus shares**; **writing off preliminary expenses**; writing off expenses, commission or discount on issue of shares/debentures; **premium payable on redemption** of preference shares or debentures; **buy-back** (s. 68). (Prescribed Ind AS companies cannot use it for some purposes VERIFY.)
- **s. 53:** shares cannot be issued at a **discount** (void) – except **sweat equity** and shares issued to creditors on conversion of debt under a statutory resolution plan/debt restructuring scheme.
- **s. 54 sweat equity:** issued to directors or employees at a discount or for consideration other than cash for know-how, IPR or value additions; **special resolution**; limits – not more than **15% of existing paid-up equity capital in a year or ₹5 crore, whichever is higher**, and total sweat equity ≤ **25%** of paid-up equity capital at any time (**50% for start-ups** up to 10 years from incorporation); **lock-in 3 years**; valuation by a registered valuer.
- **s. 55 preference shares:** only redeemable preference shares (no irredeemable); redemption within **20 years** (infrastructure projects up to **30 years**, with redemption of ≥ 10% annually from the 21st year); redeemed only out of profits or fresh issue; fully paid; CRR for redemption out of profits; premium out of profits/securities premium. A company unable to redeem may, with consent of **¾ in value** of preference shareholders and **Tribunal** approval, issue further redeemable preference shares.
- **s. 56 transfer and transmission:** a proper instrument of transfer (SH-4), stamped, dated and executed, delivered to the company within **60 days** of execution; company to deliver certificates within **one month** of receipt of the instrument (transfer) or intimation (transmission) – for listed companies, transfers only in demat form. Partly paid shares transferred on application of transferor – notice to transferee, who may object within **two weeks**.
- **s. 58 refusal to register: private company** – may refuse under its articles; must send notice of refusal within **30 days** of receipt of the instrument; appeal to the **Tribunal within 30 days of the notice** (or within **60 days** of delivery of the instrument if no notice sent). **Public company** – shares are freely transferable; transferee may appeal to the Tribunal within **60 days** of the refusal or within **90 days** of delivery if no intimation. Tribunal may order registration and rectification of register.
- **s. 61 alteration of share capital** (if articles authorise, ordinary resolution): increase, consolidate and divide (with Tribunal approval if voting percentage changes), convert into stock and reconvert, sub-divide, cancel unissued shares. **s. 64** – notice to ROC within **30 days**.
- **s. 62 further issue:** (a) **rights issue** to existing equity holders in proportion, open for **15–30 days** (notice dispatched at least **3 days** before opening; private companies may provide shorter periods if 90% of members consent); right to renounce unless articles provide otherwise; (b) to employees under **ESOP** by special resolution; (c) to any persons by **special resolution**, at a price determined by a registered valuer (for cash or other consideration). Conversion of debentures/loans into shares requires a special resolution before taking the loan.

- **s. 63 bonus shares:** out of **free reserves, securities premium or CRR**; not out of **revaluation reserve**; authorised by articles; recommended by Board and authorised in general meeting; no default in payment of interest/principal on deposits/debt securities or statutory dues to employees; partly paid shares made fully paid; **not in lieu of dividend**; once announced, cannot be withdrawn.
- **s. 66 reduction of capital:** special resolution + confirmation by the **Tribunal** (notice to Central Government, ROC, SEBI for listed companies, and creditors who may object within **3 months**); no reduction if the company is in arrears of repayment of deposits or interest.
- **s. 67:** company cannot buy its own shares (except under s. 68) or give **financial assistance** for purchase of its own or holding company's shares – exceptions: banking company lending in ordinary course; provision of money under an approved **employee share scheme** (special resolution; amount **≤ 5% of paid-up capital and free reserves**); loans to employees (other than directors/KMP) up to 6 months' salary to buy fully paid shares. Private companies meeting conditions are exempt VERIFY.

12.2 Buy-back of securities (s. 68 – 70)

- **Sources:** free reserves, securities premium, or proceeds of an issue of shares/other specified securities – but **not** out of proceeds of an earlier issue of the **same kind** of shares/securities.
- **Authorisation:** articles must authorise; **Board resolution** if buy-back ≤ **10%** of total paid-up equity capital + free reserves; **special resolution** if up to **25%**. Buy-back of **equity shares in a year ≤ 25% of total paid-up equity capital** of that year.
- **Debt–equity ratio** after buy-back ≤ **2 : 1** (secured and unsecured debts vs paid-up capital + free reserves; higher ratio if notified for a class of companies); shares fully paid; **no buy-back within one year** of the closure of a preceding buy-back offer; completed within **one year** of the resolution.
- Explanatory statement with full disclosure; **declaration of solvency** (SH-9) signed by at least two directors (one being MD) filed with ROC (and SEBI for listed); securities bought back **extinguished and physically destroyed within 7 days** of completion; register of securities bought back (SH-10); return to ROC within **30 days** (SH-11).
- **No further issue** of the same kind of shares (including allotment of new shares under s. 62(1)) within **6 months** of completion, except bonus issue and discharge of subsisting obligations (conversion of warrants, ESOP, sweat equity, conversion of preference shares/debentures).
- **Capital Redemption Reserve:** where bought back out of free reserves or securities premium, an amount equal to the **nominal value** of shares bought back is transferred to the CRR (s. 69).
- **Prohibitions (s. 70):** not through a subsidiary or investment companies; not if there is a **default in repayment of deposits, interest, redemption of debentures/preference shares, or term loans** to banks/FIs (unless default remedied and **3 years** have lapsed); not if the company has defaulted in filing annual return, dividend payment or financial statements.

12.3 Debentures (s. 71 and Rule 18)

- Debentures may be issued with an option to convert into shares – conversion requires a **special resolution**. Debentures carrying voting rights cannot be issued.
- **Secured debentures:** tenure up to **10 years** (infrastructure and certain classes up to **30 years**); secured by a charge on assets of value sufficient for repayment with interest.
- **Debenture trustee** – mandatory before a public issue of debentures or a private placement to more than **500 persons**; trust deed in SH-12 within **60 days** of allotment.
- **Debenture Redemption Reserve (DRR): not required** for all-India financial institutions, banks, **listed companies** (public issue or private placement) and listed NBFCs/HFCs; **unlisted companies** (other than NBFCs/HFCs) – **10% of outstanding value** of debentures. **Deposit/investment of 15%** of debentures maturing in the year, by **30 April**, for listed and unlisted companies (other than exempt classes) VERIFY.
- Default in redemption – Tribunal may direct redemption; punishment for officer in default.

Chapter 13: Companies Act – Acceptance of Deposits

13.1 Meaning and exclusions (Rule 2(1)(c) of the Acceptance of Deposits Rules, 2014)

Deposit includes receipt of money by way of deposit or loan or in any other form; **excluded** among others:

Not a deposit (examples)	Condition
Amounts from Central/State Government, foreign Governments, banks, public financial institutions, insurance companies	–
Amount received from another **company** (inter-corporate)	–
Share application money pending allotment	Allotted within **60 days**; else refunded within **15 days** thereafter – otherwise treated as a deposit
Amount from a **director** (or relative of a director of a private company)	Written declaration that it is not out of borrowed funds
Advance for supply of goods/services	Appropriated within **365 days** (unless subject matter of a legal proceeding)
Security deposit for performance of a contract; advances under long-term projects; advance against property under agreement	As per rule
Amount raised through issue of secured bonds/debentures; unsecured listed NCDs	Rule conditions
Amount received by a **start-up** by way of **convertible note**	**≥ ₹25 lakh in a single tranche**, convertible into equity or repayable within **10 years**
Amount received by a company from employees (non-interest bearing security deposit ≤ annual salary)	–

13.2 Who may accept and limits (s. 73, 76)

Company	From whom	Limit
Private company (s. 73(2) with exemption)	Members	Up to **100% of paid-up capital + free reserves + securities premium**; start-ups (10 years) and certain private companies – no limit VERIFY
Public company (non-eligible)	Members only	**10%** of paid-up capital + free reserves + securities premium
Eligible public company (s. 76: **net worth ≥ ₹100 crore or turnover ≥ ₹500 crore** and prior special resolution)	Members **10%** and public **25%**	Total 35%; **credit rating** required every year

Conditions (s. 73(2)): circular to members (DPT-1) and filing with ROC 30 days before issue; **Deposit Repayment Reserve** – at least **20% of the amount of deposits maturing during the following financial year**, deposited in a scheduled bank by **30 April** each year; deposit insurance (if prescribed); no default in repayment; tenure **6 months to 36 months** (deposits of 3–6 months allowed up to 10% for short-term needs); interest not above RBI ceiling for NBFCs; return of deposits (DPT-3) by **30 June**.

- **Premature repayment** (Rule 15): allowed; interest reduced by 1% from the rate applicable for the period actually run. Repayment within 6 months of acceptance not permitted except for short-term deposits VERIFY.
- **Default (s. 74, 76A):** repayment of earlier deposits/interest; Tribunal may allow time. **s. 76A** – company: fine **₹1 crore to ₹10 crore** in addition to repayment with interest; every officer in default: imprisonment up to **7 years** and fine **₹25 lakh to ₹2 crore**; if wilful with intent to deceive, also liable under **s. 447** (fraud).

Chapter 14: Companies Act – Registration of Charges

- **s. 77:** every company creating a **charge** (on property or assets in or outside India) must register it with the ROC (CHG-1; CHG-9 for debentures) within **30 days** of creation. The ROC may allow registration within **60 days** of creation on payment of additional fees, and a further **60 days** with ad valorem fees.
- **Effect of non-registration (s. 77(3)):** the charge is **not taken into account by the liquidator or any creditor** unless registered and a certificate issued – but the **debt itself remains valid** (the contract and obligation for repayment are unaffected).
- **s. 78:** if the company fails to register, the **charge-holder** may apply to the ROC; ROC gives notice to the company (14 days) and may register the charge; the charge-holder recovers the fees from the company.
- **s. 79:** modification of the terms of a charge – same procedure.
- **s. 80:** a person acquiring property subject to a registered charge is deemed to have **notice of the charge** from the date of registration.
- **s. 81, 85:** ROC maintains a register of charges open to inspection; company keeps its **register of charges** (CHG-7) at the registered office.
- **s. 82 satisfaction:** company to give intimation of payment or satisfaction within **30 days** (CHG-4); ROC issues notice to the charge-holder (14 days to show cause) and records satisfaction.
- **s. 83:** ROC may record satisfaction/release **even without intimation** from the company, on evidence that the debt has been paid or the property released; informs affected parties within 30 days.
- **s. 86 penalty:** company **₹5 lakh**; every officer in default **₹50,000**; wilful furnishing of false information – s. 447.
- **s. 87:** the Central Government may condone delay/rectify omission or misstatement in particulars, if satisfied the omission was accidental or due to inadvertence.

Chapter 15: Companies Act – Management and Administration

15.1 Registers and annual return

- **s. 88:** register of members, debenture-holders and other security holders (with index if > 50 members); kept at the registered office (or elsewhere in the same city with special resolution, under s. 94 – also any other place in India where ≥ **1/10th of members** reside).
- **s. 89, 90:** declaration of **beneficial interest** (within 30 days) and **significant beneficial owner (SBO)** – an individual who, alone or together, holds directly/indirectly **≥ 10%** of shares, voting rights or right to dividend, or exercises significant influence/control. The SBO files **BEN-1** with the company within **90 days** of acquiring such interest; the company files **BEN-2** with ROC within **30 days** of receipt; register in BEN-3. SBO Rules do not apply to holdings of IEPF, holding companies (reported holding), Central/State Government, SEBI-regulated investment vehicles (mutual funds, AIFs, REITs, InvITs) VERIFY.
- **s. 92 annual return:** in MGT-7 (MGT-7A for **OPC and small company**), filed within **60 days of the AGM** (or of the date the AGM should have been held); signed by a director and the CS (or a practising CS if no CS); listed and prescribed companies – certified by a practising CS (MGT-8). Placed on the company's website.

15.2 General meetings

Topic	Rule
AGM (s. 96)	Every company other than an **OPC** must hold an AGM each year. **First AGM within 9 months** of the end of the first financial year (need not be in the year of incorporation); subsequent AGMs within **6 months** of the end of the FY, with a gap of not more than **15 months**. ROC may extend by up to **3 months** (not for the first AGM). Held during **business hours (9 a.m. to 6 p.m.)** on a day that is **not a national holiday**, at the registered office or within the city/town/village where it is situated (unlisted company may hold anywhere in India with consent of all members in advance)
Power of Tribunal (s. 97, 98)	On default in AGM, any member may apply to the Tribunal; Tribunal may call/direct a meeting; it may direct that **one member present in person or by proxy** shall be deemed to constitute a meeting
EGM (s. 100)	Board may call; **requisition** by members holding ≥ **1/10th of paid-up capital** carrying voting rights (or ≥ 1/10th of total voting power where no share capital). Board must **call within 21 days** for a meeting to be held within **45 days** of the requisition; otherwise requisitionists may call it within **3 months**; expenses reimbursed by the company and recovered from defaulting directors. An EGM of a wholly owned subsidiary of a foreign company may be held outside India
Notice (s. 101)	At least **21 clear days** in writing or electronically. **Shorter notice:** AGM – consent of **≥ 95% of members entitled to vote**; other meetings – **majority in number** of members holding **≥ 95% of paid-up share capital** carrying voting rights (or 95% of total voting power). Notice to every member, legal representative of deceased member, assignee of insolvent member, **auditors** and every director
Explanatory statement (s. 102)	For **special business** – nature of concern/interest of directors, KMP and relatives; at AGM all business other than ordinary business (FS & reports, dividend, appointment of directors in place of those retiring, appointment/remuneration of auditors) is special
Quorum (s. 103)	**Public company: 5** members personally present if members ≤ 1,000; **15** if 1,000–5,000; **30** if > 5,000. **Private company: 2** members. If quorum not present within **half an hour**: meeting **adjourned to the same day next week**, same time and place (or as the Board decides; notice of ≥ 3 days by advertisement if day/time/place changed); a meeting called by **requisitionists stands cancelled**. At the adjourned meeting, if quorum is again not present within half an hour, **the members present shall be the quorum**
Chairman (s. 104)	Elected by members personally present on show of hands, unless articles provide otherwise
Proxies (s. 105)	Any member entitled to vote may appoint a proxy (member or not); proxy **cannot speak** and votes only on a **poll**; a person can act as proxy for **≤ 50 members** holding ≤ **10%** of total share capital with voting rights; proxy form (MGT-11) deposited **48 hours** before the meeting; inspection of proxies allowed from 24 hours before the meeting with 3 days' notice. Not applicable to company without share capital unless articles permit

Topic	Rule
Voting	**Show of hands (s. 107)** first; **e-voting (s. 108)** for listed companies and companies with ≥ 1,000 members; **poll (s. 109)** ordered by chairman or on demand by members holding **≥ 1/10th of total voting power** or holding paid-up capital of ≥ **₹5 lakh** (as prescribed); poll taken within **48 hours**; scrutinisers appointed; **postal ballot (s. 110)** for notified items
Resolutions (s. 114)	**Ordinary:** votes in favour (including casting vote) exceed votes against; **Special:** intention specified in notice, and votes in favour are **not less than three times** the votes against
Special notice (s. 115)	Required for removal of a director (s. 169), appointment of an auditor other than the retiring auditor (s. 140(4)) etc.; given by members holding **≥ 1%** of total voting power or paid-up capital of ≥ **₹5 lakh**; at least **14 days** before the meeting; company informs members at least **7 days** before
Filing (s. 117)	Special resolutions and specified agreements/Board resolutions filed in **MGT-14** within **30 days**
Minutes (s. 118)	Prepared, signed and kept within **30 days** of the meeting; evidence of proceedings
Report on AGM (s. 121)	Listed public company – MGT-15 within **30 days** of AGM
OPC (s. 122)	AGM, quorum and certain provisions not applicable; resolutions communicated by the member and entered in the minute book

REMEMBER **Adjourned meeting with only one member present**

the institute's position in its suggested answers: validity is tested under **s. 103** – if quorum is again not present within half an hour at the adjourned meeting, **the members present shall be the quorum**, so resolutions passed there bind all members. Separately, a meeting ordinarily needs at least two persons (*Sharp v. Dawes*), with exceptions: **OPC**, a **class meeting** where one person holds all shares of the class, and a meeting ordered by the **Tribunal/Central Government** with a direction that one member present is deemed to constitute a meeting (s. 97, 98).

15.3 Board meetings (brief)

- First Board meeting within **30 days** of incorporation; at least **4 meetings a year**, gap ≤ **120 days** (OPC/small/dormant company – at least one meeting in each half of the year with a gap of ≥ 90 days); notice **7 days**; quorum **one-third of total strength or 2 directors, whichever is higher** (s. 173–174).

15.4 Resolutions and agreements to be filed with the ROC (s. 117)

Filed in **Form MGT-14** within **30 days**: (a) **special resolutions**; (b) resolutions agreed to by **all members** which would otherwise need a special resolution; (c) resolutions of the Board on **appointment, re-appointment or variation of terms of a managing director**; (d) resolutions or agreements binding **a class of members**; (e) resolutions requiring **unanimous consent** of members; (f) **Board resolutions under s. 179(3)** (calls, buy-back, issue of securities, borrowing, investments, loans, approval of financial statements and Board's report, diversification, amalgamation, takeover) VERIFY; (g) resolutions for **voluntary winding up**; and (h) any other prescribed resolution. Private companies are exempt from filing certain s. 179(3) resolutions VERIFY.

- **Service of notice in electronic mode (s. 20, Rule 35 of Management and Administration Rules):** a company may send documents and notices of meetings by **e-mail** to the address registered with the company or depository; the notice is deemed served at the time of transmission; the subject line states the company's name and the purpose; members may opt for physical copies.

Chapter 16: Companies Act – Declaration and Payment of Dividend

- **Dividend** (s. 2(35)) includes interim dividend.
- **Sources (s. 123(1)):** (a) **profits of the current year after depreciation** (s. 123(2) and Schedule II), after transfer to reserves as the company thinks fit; (b) **profits of previous years** after depreciation remaining undistributed; (c) both; (d) money provided by the Central/State Government for payment of dividend in pursuance of a guarantee. Unrealised/notional gains, revaluation of assets and fair-value changes **cannot** be used.
- **Dividend out of accumulated profits when there is inadequate profit (Rule 3 of the Declaration and Payment of Dividend Rules):** rate ≤ **average of the three preceding years**; amount drawn ≤ **1/10th of paid-up capital + free reserves**; first set off current-year losses; balance of reserves after drawal ≥ **15% of paid-up capital**.
- **Interim dividend (s. 123(3)):** declared by the **Board** during the FY or up to the AGM, out of surplus in P&L and/or profits of the FY for which it is declared/generated up to the quarter preceding declaration. If the company has incurred a **loss** up to the end of the quarter immediately preceding declaration, interim dividend ≤ **average rate of the three preceding FYs**.
- **Separate bank account:** dividend amount (including interim) deposited within **5 days** of declaration.
- **Payment:** only to the **registered shareholder**, to his order or to his banker; **in cash** (cheque, warrant or electronic mode) – capitalisation of profits as fully paid bonus shares or paying up unpaid amounts is permitted, but **bonus cannot be issued in lieu of dividend**.
- **Who declares final dividend:** members at the AGM **on the recommendation of the Board**; members **cannot increase** the rate recommended by the Board (Table F, regulation 80), but may reduce it.
- **No dividend on equity shares (s. 123(6))** while the company has failed to comply with ss. 73–74 (acceptance/repayment of deposits) – for so long as the failure continues.
- **Unpaid dividend (s. 124):** dividend not paid/claimed within **30 days** of declaration – transfer within **7 days** after the expiry of that 30-day period to an **Unpaid Dividend Account** in a scheduled bank; statement on the website within 90 days; amounts unpaid for **7 years** transferred to the **Investor Education and Protection Fund (IEPF)**, along with **shares** on which dividend has been unpaid/unclaimed for **7 consecutive years**. Default – interest @ **12% p.a.** on the amount not transferred; penalty on company ₹1 lakh and officer ₹25,000.
- **s. 127 punishment for failure to distribute within 30 days:** directors – imprisonment up to **2 years** and fine ≥ **₹1,000 per day** of default; company – simple interest @ **18% p.a.** for the period of default. **No offence** where: dividend could not be paid by operation of law; shareholder's directions could not be complied with; dispute about the right to receive; dividend lawfully adjusted against a sum due from the shareholder; failure not due to default of the company.

Chapter 17: Companies Act – Accounts of Companies

17.1 Books of account (s. 128)

- Kept at the **registered office** – the Board may decide to keep them at **another place in India**; company files the full address with the ROC within **7 days** of the decision (AOC-5).
- **Branch** office books may be kept at the branch, with **proper summarised returns** sent periodically to the registered office.
- Kept on **accrual basis** and **double entry** system; may be kept in **electronic mode** – accessible in India at all times; **daily back-up** on servers physically located in India; service-provider details furnished to ROC yearly.
- Open to **inspection by directors** during business hours (for a subsidiary, by a person authorised by the Board).
- Preserved for **8 years** immediately preceding the FY (or from incorporation if shorter); Central Government may direct longer where investigation is ordered.
- Responsibility: MD, WTD in charge of finance, CFO or any person charged by the Board – penalty ₹50,000 for contravention.

17.2 Financial statements, re-opening and revision

- **s. 129:** FS give a **true and fair view**, comply with notified **accounting standards** and **Schedule III**; **consolidated FS** where the company has subsidiaries/associates/JVs, with a statement of salient features in **AOC-1**.
- **s. 130 re-opening of accounts (involuntary):** only on an order of a **court or Tribunal**, on application by the **Central Government, Income-tax authorities, SEBI, any other statutory regulatory body or any person concerned**, on grounds that the relevant earlier accounts were prepared in a **fraudulent manner** or the **affairs were mismanaged** casting doubt on reliability. Not beyond **8 years** before the current FY. Notice to the Central Government, Income-tax authorities, SEBI etc.
- **s. 131 voluntary revision:** if directors think FS or Board's report do not comply with s. 129/134, they may prepare revised FS/report for any of the **three preceding financial years**, after **approval of the Tribunal** (notice to Central Government and Income-tax authorities); revision **not more than once in a financial year**; detailed reasons disclosed in the Board's report of the relevant FY; revisions confined to the non-compliance.

17.3 Board's report (s. 134) and approval

- FS approved by the **Board** and signed by the **chairperson** (if authorised) or by **two directors** (one being MD), and the **CEO, CFO and CS** where appointed; OPC – one director.
- Board's report includes: web-link of annual return, number of Board meetings, **directors' responsibility statement**, independent directors' declaration, policy on directors' appointment, explanations on auditor's qualifications, loans/investments (s. 186), related party contracts (AOC-2), state of affairs, transfer to reserves, dividend, material changes after balance sheet date, conservation of energy/technology/forex, risk management policy, CSR policy and initiatives, annual evaluation (listed and prescribed), details of frauds (other than those reported to the Central Government), and **(from 14 July 2025)** number of **sexual-harassment complaints** received, disposed of and pending beyond 90 days and a **statement of compliance with the Maternity Benefit Act, 1961**.
- **Small company and OPC:** abridged Board's report.
- Copies to members at least **21 days** before the AGM (s. 136) – listed companies keep FS of subsidiaries on the website; filing with ROC within **30 days of AGM** (s. 137) in **AOC-4** (CFS – AOC-4 CFS; XBRL for prescribed companies); OPC within **180 days** from the close of FY. Unadopted FS filed within 30 days of AGM as provisional; adopted FS within 30 days of the adjourned AGM.

17.4 Corporate Social Responsibility (s. 135)

- **Applicable** to every company having, in the **immediately preceding financial year**, **net worth ≥ ₹500 crore** or **turnover ≥ ₹1,000 crore** or **net profit ≥ ₹5 crore** (foreign company branches too).
- **CSR committee** of ≥ 3 directors including **one independent director** (where required); unlisted/private companies without independent directors – 2 directors. If CSR obligation ≤ **₹50 lakh**, the Board itself discharges the functions; no committee needed.

- **Spend at least 2% of average net profits** (s. 198 profits) of the **three immediately preceding FYs** (or since incorporation); preference to local areas. **Excess spent** may be set off against requirements of up to the **next 3 FYs** (excludes surplus from CSR activities).
- **Unspent amount:** relating to an **ongoing project** – transfer to an **Unspent CSR Account** within **30 days** of end of FY, to be spent within **3 FYs**, else transfer to a **Schedule VII fund** within 30 days of completion of the third FY; **other** unspent amounts – transfer to a Schedule VII fund (e.g. PM's National Relief Fund) within **6 months** of the end of the FY.
- **Impact assessment** by an independent agency for companies with average CSR obligation ≥ **₹10 crore** in the preceding three years for projects ≥ ₹1 crore (projects through ZCZP instruments exempt from 27 May 2026).
- **New (May 2026):** contribution to **Zero Coupon Zero Principal instruments** issued by not-for-profit organisations on a **Social Stock Exchange** counts as CSR – capped at **10%** of the company's total CSR expenditure for the FY.
- Non-compliance: company – twice the unspent amount or ₹1 crore, whichever is less; officer in default – 1/10th of the unspent amount or ₹2 lakh, whichever is less.

17.5 Internal audit (s. 138, Rule 13 Accounts Rules)

Mandatory for: every **listed** company; **unlisted public** company with paid-up capital ≥ **₹50 crore**, or turnover ≥ **₹200 crore**, or outstanding loans/borrowings from banks/PFIs ≥ **₹100 crore**, or outstanding deposits ≥ **₹25 crore** (any time in preceding FY); **private** company with turnover ≥ **₹200 crore** or borrowings ≥ **₹100 crore**. Internal auditor – a CA/CMA or other professional decided by the Board, may or may not be an employee.

Chapter 18: Companies Act – Audit and Auditors

18.1 Appointment (s. 139)

Situation	Who appoints	Time limit / term
First auditor – non-Government company	**Board**	Within **30 days** of registration; if Board fails – members at an **EGM within 90 days**; holds office till the conclusion of the **first AGM**
Subsequent auditor	**Members at the first AGM** (individual or firm)	Holds office from the conclusion of that meeting till the conclusion of the **sixth AGM** (term of 5 years); written consent and eligibility certificate obtained; company files **ADT-1** within **15 days** of the meeting
First auditor – Government company	**C&AG**	Within **60 days** of registration; if C&AG fails – Board within next 30 days; if Board fails – members at EGM within 60 days
Subsequent – Government company	**C&AG**	Within **180 days** from the commencement of the FY; till the conclusion of the AGM
Casual vacancy – non-Government	**Board** within **30 days**	If caused by **resignation** – appointment also approved by the company in a general meeting within **3 months** of the Board's recommendation; holds office till the conclusion of the next AGM
Casual vacancy – Government company	**C&AG** within **30 days**	Else Board within next 30 days

- **Rotation (s. 139(2))** – applies to **listed companies** and prescribed classes: **unlisted public companies with paid-up capital ≥ ₹10 crore**; **private companies with paid-up capital ≥ ₹50 crore**; all companies (other than above) with **public borrowings from FIs/banks or public deposits ≥ ₹50 crore** (OPC and small companies excluded). An **individual** may not be appointed for more than **one term of 5 consecutive years**; an **audit firm** for more than **two terms of 5 consecutive years**; **cooling-off period of 5 years** after completion of the term(s). Firms with common partners also barred.
- Where the company has an **audit committee**, every appointment is made after considering its recommendations (s. 177).
- **Joint auditors** may be appointed; members may also require rotation of the audit partner.

18.2 Removal, resignation (s. 140)

- **Removal before expiry of term: special resolution** + prior approval of the **Central Government** (application in ADT-2 within 30 days of Board resolution; special resolution within **60 days** of CG approval); auditor given a reasonable opportunity of being heard.
- **Resignation:** auditor files **ADT-3** with the company and ROC within **30 days** stating reasons; for Government companies also with C&AG.
- **Appointment of an auditor other than the retiring auditor** at the AGM requires **special notice** (s. 115); copy sent to the retiring auditor, who may make written representations (read out at the meeting if not circulated).
- **Tribunal** (on its own or on application by CG or any person concerned) may direct change of auditor who acted fraudulently or abetted fraud; such auditor not eligible for **5 years**; also liable under s. 447.

18.3 Eligibility, qualifications and disqualifications (s. 141)

- Only a **chartered accountant in practice**, or a **firm** whereof majority of partners practising in India are qualified (only those partners sign). An **LLP** of chartered accountants can be appointed.
- **Not eligible:** (a) a **body corporate** (other than an LLP); (b) an **officer or employee** of the company; (c) a person who is a **partner, or in employment, of an officer or employee** of the company; (d) a person who, **or whose relative or partner**, (i) holds any **security or interest** in the company/subsidiary/holding/associate/fellow subsidiary (relative may hold up to **₹1 lakh face value**), (ii) is **indebted** to the company (or its group) above **₹5 lakh**, or (iii) has given a **guarantee or security** for any third person's indebtedness to the company above **₹1**

lakh; (e) a person or firm having a **business relationship** with the company (other than commercial transactions in the ordinary course of business at arm's length, or professional services permitted); (f) a person whose **relative is a director or KMP**; (g) a person in **full-time employment elsewhere**, or a person/partner holding appointment as auditor of more than **20 companies** (excluding OPC, dormant, small and private companies with paid-up capital < ₹100 crore); (h) a person **convicted of an offence involving fraud** within **10 years**; (i) a person who renders **prohibited services** (s. 144) directly or indirectly to the company/holding/subsidiary.

- If an auditor becomes **disqualified after appointment**, he **vacates office** and the vacancy is a casual vacancy (s. 141(4)).

18.4 Powers, duties and other provisions

- **s. 142 remuneration:** fixed in general meeting (or as determined there); first auditor's by the Board; includes expenses but not fees for other services.
- **s. 143 powers and duties:** right of **access at all times** to books and vouchers (also those of subsidiaries for CFS); entitled to information and explanations; enquiries into loans and advances, book entries, sale of investments at less than cost, loans shown as deposits, personal expenses charged to revenue, cash received for shares allotted. Report to members on whether FS give a **true and fair view**, with matters in s. 143(3) (information obtained, proper books, adverse observations, director disqualification under s. 164(2), internal financial controls, pending litigations, IEPF transfers etc.), and **CARO** where applicable. Government company – C&AG may direct, conduct **supplementary audit** within **60 days** of receipt of the audit report and comment.
- **Fraud reporting (s. 143(12), Rule 13 Audit Rules):** fraud involving **₹1 crore or above** – report to the **Board/audit committee within 2 days** of knowledge seeking reply within **45 days**; auditor forwards the report with the reply/observations to the **Central Government within 15 days** of receipt of reply (or of the expiry of 45 days) in **Form ADT-4, filed electronically** (from 14 July 2025). Fraud **below ₹1 crore** – reported to the audit committee/Board within 2 days, disclosed in the **Board's report**. Applies also to cost accountants and company secretaries in practice conducting cost/secretarial audit. Penalty for not reporting – listed company ₹5 lakh; other company ₹1 lakh.
- **s. 144 prohibited services:** accounting and book-keeping; internal audit; design and implementation of any financial information system; actuarial; investment advisory; investment banking; rendering of outsourced financial services; management services; any other prescribed service – rendered directly or through relatives, partners, associate entities, to the company, its holding or subsidiary. Other services require **Board/audit committee approval**.
- **s. 145:** auditor signs the report; qualifications/adverse remarks read at the general meeting and open to inspection.
- **s. 146:** notice of general meetings to the auditor; auditor (or authorised representative who is qualified to be auditor) attends unless exempted and has a right to be heard on any part of the business concerning him as auditor.
- **s. 147 punishment:** company ₹25,000–₹5 lakh; officer in default ₹10,000–₹1 lakh; auditor contravening ss. 139, 143, 144, 145 – ₹25,000 to ₹5 lakh or 4 times the remuneration, whichever is less; wilful contravention to deceive – imprisonment up to 1 year and fine ₹50,000 to ₹25 lakh or 8 times the remuneration, whichever is less; refund of remuneration and damages.
- **s. 148 cost audit:** Central Government may direct for specified companies; cost auditor (cost accountant) appointed by the Board on audit committee recommendation, remuneration ratified by members; report within **180 days** from the end of FY VERIFY; statutory auditor cannot be cost auditor.

18.5 Matters the auditor must inquire into (s. 143(1))

The auditor has a right of access to books and vouchers and must **inquire** into: (a) whether **loans and advances** made on the basis of security are **properly secured** and their terms are not **prejudicial** to the company or its members; (b) whether transactions represented merely by **book entries** are prejudicial to the company; (c) where the company is **not an investment or banking company**, whether assets in the form of shares, debentures and securities have been **sold at a price less than their cost**; (d) whether **loans and advances** have been shown as **deposits**; (e) whether **personal expenses** have been charged to the revenue account; and (f) where shares have been **allotted for cash**, whether cash has actually been received, and if not, whether the books and balance sheet are correct and not misleading.

Chapter 19: Companies Act – Directors, Key Managerial Personnel and Rights of Shareholders

19.1 Board of directors – composition (s. 149)

Requirement	Provision
Minimum / maximum	Public company **3**, private company **2**, OPC **1**; maximum **15** (more by **special resolution**)
Woman director	Every **listed** company and every public company with paid-up capital ≥ **₹100 crore** or turnover ≥ **₹300 crore** – at least one woman director VERIFY
Resident director	At least one director who has stayed in India for **182 days or more** in the financial year
Independent directors	Listed public company – at least **one-third** of total directors; public companies with paid-up capital ≥ ₹10 crore, or turnover ≥ ₹100 crore, or outstanding loans, debentures and deposits > ₹50 crore – at least **2** VERIFY. Term up to **5 consecutive years**; re-appointment for one more term by **special resolution**; then **3-year cooling-off**

19.2 Appointment of directors

- **DIN** (s. 153–159): an individual must hold a Director Identification Number; only **one DIN** for life; consent to act in **Form DIR-2** filed with the ROC within 30 days of appointment.
- **First directors** – named in the articles; if not named, subscribers to the memorandum who are individuals are deemed first directors until directors are appointed.
- **Appointment in general meeting** (s. 152) – at least **two-thirds** of the directors of a public company are **liable to retire by rotation**; at every AGM **one-third** of them retire (longest in office first) and are eligible for re-appointment. Each director is appointed by a **separate resolution** (s. 162) unless the meeting unanimously agrees otherwise.
- **Additional director** (s. 161(1)) – by the Board if the articles permit; holds office **up to the next AGM** or the last date on which the AGM should have been held.
- **Alternate director** (s. 161(2)) – for a director absent from India for **at least 3 months**; vacates office when the original director returns.
- **Casual vacancy** (s. 161(4)) – in a public company, filled by the Board; the new director holds office until the original director's term would have ended.
- **Nominee director** (s. 161(3)) – appointed by an institution, under an agreement, or by the Government.

19.3 Disqualifications (s. 164) and number of directorships (s. 165)

LEGAL PROVISION Disqualifications for appointment as director – s. 164(1)

A person cannot be appointed a director if he: (a) is of **unsound mind** as declared by a competent court; (b) is an **undischarged insolvent**; (c) has **applied to be adjudicated an insolvent** and the application is pending; (d) has been **convicted** of an offence and sentenced to imprisonment of at least **6 months**, and 5 years have not passed since the end of the sentence (if sentenced to **7 years or more**, he can never be appointed); (e) is disqualified by an **order of a court or Tribunal** in force; (f) has **not paid calls** on shares held by him for **6 months** from the last date fixed; (g) has been convicted of an offence dealing with **related party transactions** (s. 188) in the preceding 5 years; (h) has **not obtained a DIN**; or (i) has accepted directorships beyond the limit in s. 165(1).

s. 164(2): a director of a company that (a) has **not filed financial statements or annual returns for 3 continuous financial years**, or (b) has failed to **repay deposits, redeem debentures, or pay interest or declared dividend for one year or more**, cannot be re-appointed in that company or appointed in any other company for **5 years**.

A **private company** may add other disqualifications in its articles (s. 164(3)).

- **s. 165:** a person may be a director in at most **20 companies**, of which not more than **10 public companies** (private companies that are holding or subsidiary of a public company count as public). Dormant companies are excluded VERIFY.

19.4 Duties, vacation, resignation and removal

Topic	Provision
Duties (s. 166)	Act according to the **articles**; act in **good faith** to promote the objects of the company for the benefit of members, employees, community and environment; exercise **due and reasonable care, skill, diligence** and independent judgement; avoid **conflict of interest**; no **undue gain** (else pay it to the company); **not assign** his office. Penalty ₹1 lakh to ₹5 lakh
Vacation (s. 167)	Office vacated if he incurs a s. 164 disqualification; **absents himself from all Board meetings for 12 months** with or without leave; acts against s. 184 (interest); is disqualified by court; is **convicted** and sentenced to at least 6 months; is removed under the Act; or ceases to hold the office or employment in a holding/subsidiary company because of which he was appointed
Resignation (s. 168)	By written notice to the company; effective from the date the notice is **received** or a later date specified in it. The company files **DIR-12** with the ROC within **30 days**; the director may also file **DIR-11** with reasons. He remains liable for offences during his tenure
Removal (s. 169)	By **ordinary resolution** of members, after **special notice** (s. 115 – at least **14 days** before the meeting); the director has a right to be **heard** and to make a **written representation**. Not applicable to a director appointed by the Tribunal under s. 242. The vacancy may be filled at the same meeting

19.5 Meetings and powers of the Board

- **Board meetings (s. 173):** first meeting within **30 days** of incorporation; at least **4 meetings a year** with a gap of not more than **120 days** between two meetings (OPC, small and dormant companies: at least one in each half of the calendar year, gap ≥ 90 days). **Notice of at least 7 days**; video-conferencing allowed.
- **Quorum (s. 174): one-third** of total strength or **2 directors**, whichever is higher.
- **Circular resolution (s. 175):** passed by circulating the draft to all directors; approved by a majority of directors entitled to vote; unless one-third of directors require it to be decided at a meeting.
- **Powers only at Board meetings (s. 179(3)):** make **calls** on unpaid shares; authorise **buy-back** (s. 68); issue securities; **borrow** money; **invest** funds; grant **loans** or give guarantees; approve **financial statements and the Board's report**; diversify the business; approve amalgamation, merger or reconstruction; take over a company or acquire a controlling stake.
- **Restrictions (s. 180):** the Board needs a **special resolution** to (a) sell, lease or dispose of the whole or substantially the whole of an undertaking, (b) invest compensation received on a merger, (c) **borrow** where total borrowings would exceed paid-up capital + free reserves + securities premium (excluding temporary loans), and (d) remit or give time for repayment of a debt due from a director.
- **Disclosure of interest (s. 184):** at the first Board meeting of every financial year and on any change, in **Form MBP-1**; an interested director must not take part in the discussion or vote.

19.6 Managerial personnel and KMP

- **KMP – s. 2(51):** (i) CEO or MD or manager; (ii) **company secretary**; (iii) **whole-time director**; (iv) **CFO**; (v) any other officer not more than one level below the directors, in whole-time employment, designated as KMP by the Board; and (vi) other prescribed officers.
- **s. 203:** every **listed company** and every public company with paid-up share capital of **₹10 crore or more** must have whole-time KMP – (a) MD or CEO or manager (or a whole-time director), (b) company secretary and (c) CFO. A whole-time KMP cannot hold office in more than one company at the same time (except a subsidiary). A vacancy must be filled by the Board within **6 months**.
- **MD / WTD / manager (s. 196):** term not more than **5 years** at a time; age **21 to 70** (beyond 70 by special resolution with justification).
- **Managerial remuneration (s. 197):** a public company's total managerial remuneration ≤ **11%** of net profits (s. 198). One MD/WTD/manager ≤ **5%**; if more than one, all together ≤ **10%**. Non-executive directors ≤ **1%** (if there is an MD/WTD/manager) or **3%** otherwise. Higher limits need a **special resolution**.

19.7 Operational and financial control; internal financial control (s. 134, 143, 177)

- **Directors' responsibility statement – s. 134(5):** the Board's report states that the directors (a) followed applicable accounting standards, (b) selected and applied accounting policies consistently and made reasonable judgements, (c) took proper care in maintaining records, (d) prepared accounts on a **going-concern** basis, (e) for a **listed company**, laid down **internal financial controls** that are adequate and operating effectively, and (f) devised systems to ensure compliance with all laws.
- **IFC** means the policies and procedures adopted for orderly and efficient conduct of business, safeguarding of assets, prevention and detection of frauds and errors, accuracy and completeness of records, and timely preparation of reliable financial information (Rule 8(5)(viii) of the Accounts Rules).
- **Auditor's report – s. 143(3)(i):** whether the company has adequate IFC with reference to financial statements and their **operating effectiveness**. Not required for OPCs, small companies, and private companies with turnover < **₹50 crore** and borrowings < **₹25 crore** VERIFY.
- **Audit committee – s. 177:** every listed public company and prescribed public companies; at least **3 directors with independent directors forming a majority**; most members including the chairperson able to read and understand financial statements. Functions: recommend appointment and remuneration of auditors; review the auditor's **independence** and the audit process; examine financial statements and the auditor's report; approve **related party transactions**; scrutinise inter-corporate loans and investments; valuation of assets where necessary; **evaluate IFC and risk management**; monitor end use of funds raised. It also oversees the **vigil mechanism** (s. 177(9)–(10)).

19.8 Rights of shareholders

Right	Provision
Voting	Every equity shareholder has a vote on every resolution in proportion to his share of paid-up equity capital (s. 47); vote by proxy (s. 105), e-voting and postal ballot
Notice and attendance	Receive notice of general meetings (s. 101), attend and speak
Information	Copies of financial statements (s. 136); inspect registers and minutes (s. 94, 119)
Dividend	Receive declared dividend within **30 days** of declaration (s. 127)
Further issue	**Rights issue** in proportion to holding (s. 62)
Transfer	Shares are movable property, transferable as per articles (s. 44, 56)
Requisition	Members holding **one-tenth** of paid-up voting capital can requisition an **EGM** (s. 100)
Remedies	Apply to NCLT for relief against **oppression and mismanagement** (s. 241) – at least **100 members** or **one-tenth** of members or holders of one-tenth of issued share capital (s. 244); **class action** (s. 245)
Winding up	Share in surplus assets after creditors are paid

19.9 Points frequently examined

- **Remuneration for professional services (s. 197(4)):** remuneration for services rendered by a director **in any other capacity** is **not included** in the managerial remuneration limits if (a) the services are of a **professional nature**, and (b) in the opinion of the **Nomination and Remuneration Committee** (or the Board) the director **possesses the requisite qualification** for the practice of the profession. So a qualified director's professional bill can be paid outside the 11% limit.
- **Woman director vacancy (Rule 3, Appointment and Qualification of Directors Rules):** an intermittent vacancy of a woman director must be filled by the Board **at the earliest but not later than the immediate next Board meeting or 3 months from the date of vacancy, whichever is later**.
- **Director appointed in place of a removed director (s. 169(5)–(6)):** holds office only until the date up to which the removed director would have held office.
- **Resignation (s. 168):** effective from the date of receipt of the notice by the company or the date specified, whichever is later; the director remains **liable for offences** during his tenure even after resignation. Filing of DIR-11 by the director is optional; the company must file DIR-12.

Chapter 20: Business Ethics and Emotional Intelligence

20.1 Ethics – meaning, nature and importance

Ethics is the set of moral principles that decides what is **right and wrong** in human conduct. **Business ethics** applies these principles to business decisions – towards customers, employees, investors, suppliers, government and society.

- **Nature:** (1) a **code of conduct** based on moral values; (2) relative – varies with time, culture and situation, though core values are universal; (3) **voluntary** – self-discipline rather than legal compulsion; (4) based on **social customs** and values; (5) concerned with **human behaviour**; (6) a **normative** science – it prescribes what ought to be; (7) applies at the level of the individual and the organisation; (8) requires **education and guidance**.
- **Importance / relevance to business:** builds **trust and goodwill**; long-term profitability and survival; customer loyalty; attracts and retains employees; protects investors; avoids legal trouble and penalties; better decision-making; social responsibility and sustainable development; good corporate governance.

20.2 The Seven Principles of Public Life (Nolan principles)

Set out by the **Nolan Committee** (UK Committee on Standards in Public Life, 1995):

Principle	Meaning
Selflessness	Act solely in terms of the public interest
Integrity	Avoid placing oneself under any obligation to people or organisations that might influence one's work; do not act to gain financial or other benefits
Objectivity	Act and take decisions impartially, fairly and on merit, using the best evidence and without discrimination or bias
Accountability	Be accountable to the public for decisions and actions and submit to scrutiny
Openness	Act and take decisions in an open and transparent manner; withhold information only for clear and lawful reasons
Honesty	Be truthful
Leadership	Exhibit these principles in one's own behaviour, promote and support them, and challenge poor behaviour

20.3 Ethics and law

Basis	Law	Ethics
Source	Made by the State (legislature, courts)	Arises from conscience, society, culture and religion
Enforcement	Enforced by courts with penalties	Self-imposed; social disapproval only
Nature	Written, specific	Mostly unwritten, broad
Scope	Minimum standard of behaviour	Higher standard – what *ought* to be done
Change	By amendment	Evolves with social values

Law and ethics **overlap**: many laws (anti-fraud, consumer protection) are based on ethical values, but an act can be **legal yet unethical** (e.g., aggressive tax avoidance that defeats the intent of the law) or **ethical but illegal** in rare cases. A professional must comply with law **and** follow ethics.

20.4 Values and attitudes of professional accountants

- **Fundamental principles** (Code of Ethics): **integrity**, **objectivity**, **professional competence and due care**, **confidentiality** and **professional behaviour**.
- **Values:** honesty, independence, fairness, transparency, accountability, commitment to public interest, continuous learning.
- **Attitudes:** professional scepticism, responsibility, respect for others, willingness to say "no" to pressure, and a questioning mind.
- **Threats** to compliance: self-interest, self-review, advocacy, familiarity and intimidation; safeguards: professional standards, review, rotation, disclosure, declining the engagement.

20.5 Primary norms of business ethics and their application

Norm	Application
Honesty	Truthful advertising, true and fair accounts, no window dressing
Accountability	Accept responsibility for decisions; report to stakeholders
Fairness / justice	Fair wages, non-discrimination, fair pricing
Integrity	Keep promises, avoid conflicts of interest and bribery
Respect for others	Dignity of employees, privacy of customer data
Compliance with law	Taxes, environment, labour and company laws

- **Decisions regarding employers/employees:** fair recruitment and promotion, safe workplace, no harassment, whistle-blower protection, honest appraisal.
- **Finance:** accurate financial reporting, no insider trading, no misuse of funds, prudent risk-taking, fair dealing with lenders and investors.
- **Trading:** no hoarding, adulteration, under-weighing, black-marketing or misleading advertisement; fair competition; honouring contracts.

20.6 Ethical dilemmas and decision-making

An **ethical dilemma** arises where a choice must be made between two courses of action, each with ethical arguments (e.g., loyalty to employer vs duty to the public). A structured approach: (1) identify the facts and the stakeholders; (2) identify the ethical issues and the principles involved; (3) consider the **law** and the organisation's code of conduct; (4) list alternative courses and their consequences; (5) consult (superiors, ethics committee, professional body); (6) choose and act; (7) document and review.

20.7 Emotional intelligence (EI)

Emotional intelligence is the ability to **recognise, understand and manage one's own emotions** and to **recognise and influence the emotions of others**. The concept was popularised by **Daniel Goleman** (1995); the term was first used by Salovey and Mayer.

Component (Goleman)	Meaning
Self-awareness	Knowing one's emotions, strengths, weaknesses and their effect on others
Self-regulation	Controlling impulses and moods; thinking before acting
Motivation	Inner drive to achieve beyond money or status; optimism
Empathy	Understanding others' emotions and viewpoints
Social skills	Managing relationships, building networks, influencing and leading

- **EQ vs IQ:** IQ measures cognitive ability (reasoning, memory); EQ measures emotional and social competence. IQ helps you get a job; **EQ helps you succeed and lead** in it. EQ can be developed through practice.
- **Effects of EI: work** – better teamwork, leadership, conflict handling and decisions; **physical health** – lower stress, blood pressure and burnout; **mental health** – less anxiety and depression, more resilience; **relationships** – better communication, trust and empathy.
- **Relevance to ethics:** EI helps a professional resist pressure, handle ethical dilemmas calmly and show empathy towards stakeholders.

20.8 Other points frequently examined

- **CFA Institute Code of Ethics** – members must: (1) act with **integrity, competence, diligence and respect** in an ethical manner with the public, clients, employers and colleagues; (2) place the **integrity of the profession** and the interests of clients above their own; (3) use **reasonable care and independent professional judgement**; (4) practise and encourage others to practise professionally and ethically; (5) promote the **integrity and viability of the global capital markets**; and (6) maintain and improve their **professional competence** VERIFY.
- **Kinds of business ethics:** personal responsibility, corporate responsibility, loyalty, respect for others, **fairness**, **transparency**, **trustworthiness**, technology and data ethics, environmental and social responsibility.

- **Unethical practices** by executives: insider trading; **window dressing** and false accounts; bribery and kickbacks; misuse of company assets; discrimination and harassment; misleading advertising; tax evasion; environmental violations; leaking confidential data.
- **Themes for designing management accounting systems** (also examined in this module): **customer focus**, **value-chain and supply-chain analysis**, **key success factors** (cost and efficiency, quality, time, innovation), and **continuous improvement and benchmarking** (e.g., kaizen costing) VERIFY.

Number and section sheet

Topic	Remember
Contract	s. 2(h) contract; s. 10 essentials; s. 11 capacity; s. 13–22 consent (15 coercion, 16 undue influence, 17 fraud, 18 misrepresentation, 20–22 mistake); s. 25 exceptions to "no consideration"; s. 26–30 void agreements; s. 31–36 contingent; s. 56 impossibility; s. 62 novation; s. 68–72 quasi-contracts; s. 73 damages; s. 124 indemnity; s. 126 guarantee; s. 148 bailment; s. 172 pledge; s. 182 agency
Sale of Goods	s. 4 sale vs agreement to sell; s. 12 condition/warranty; s. 14–17 implied conditions; s. 16 caveat emptor; s. 18–24 transfer of property; s. 27 nemo dat; s. 45 unpaid seller; s. 47 lien; s. 50 stoppage in transit; s. 54 resale; s. 64 auction
NI Act	s. 4 promissory note; s. 5 bill; s. 6 cheque; s. 9 holder in due course; s. 87 material alteration; s. 123–131 crossing; **s. 138** – notice within **30 days** of information of dishonour, payment within **15 days**, complaint within **1 month**; punishment up to **2 years** or fine up to **twice** the amount; s. 143A interim compensation up to **20%**
Partnership / LLP	Partnership max **50** partners (Companies Rules); s. 69 effects of non-registration; s. 40–44 dissolution. LLP: min **2** partners, at least **2 designated partners** (one resident in India); consent of designated partner – **Form 9**
Factories	10 workers with power / 20 without; 48 h/week, 9 h/day, spread-over 10½ h, rest after 5 h; overtime 2×; child < 14 barred; canteen > 250; creche > 30 women; welfare officer ≥ 500; ambulance room > 500; leave 1 day per 20 days (240-day rule)
Gratuity / EPF / ESI	Gratuity: 10 employees, 5 years, 15/26 × wages × years, ₹20 lakh. EPF: 20 persons, 12% + 12%, EPS 8.33%. ESI: 10 persons, ₹21,000 wages, 3.25% + 0.75%
Code on Wages	4 Acts merged; 50% wage rule; deductions ≤ 50%; monthly wages by 7th; bonus 8.33%–20%, 30 days' work
Companies Act	Private ≤ 200 members; small company paid-up ≤ **₹10 crore** and turnover ≤ **₹100 crore** (from 1-12-2025); buy-back ≤ 25% (Board 10%), debt-equity ≤ 2:1; charge registration 30 days; AGM – first within 9 months, then gap ≤ 15 months; notice 21 clear days; dividend paid within 30 days; unpaid dividend to special account within 7 days after 30 days; IEPF after 7 years; books kept 8 years; CSR – net worth ₹500 crore / turnover ₹1,000 crore / net profit ₹5 crore, 2% of average net profit
Directors	Min 3/2/1, max 15; resident 182 days; 20 companies (10 public); retirement by rotation 2/3 and 1/3; Board meetings 4 a year, gap ≤ 120 days; quorum 1/3 or 2; removal by ordinary resolution with special notice (14 days); KMP – listed or paid-up ≥ ₹10 crore; managerial remuneration 11% / 5% / 10% / 1% / 3%

Common mistakes in answers

1. Writing the general law without the **section number** – examiners give a mark for the correct section.
2. Not stating a **conclusion** in case-based questions (valid/void, liable/not liable).
3. Confusing **void** and **voidable** agreements, and **condition** and **warranty**.
4. Mixing **sale** with **agreement to sell**, and **lien** with **stoppage in transit**.
5. In s. 138 cases, forgetting the **time limits** (30 days / 15 days / 1 month).
6. Using outdated company-law limits – e.g. small company **₹4 crore / ₹40 crore** has been replaced by **₹10 crore / ₹100 crore**.
7. Treating removal of a director as needing a special resolution – it needs an **ordinary resolution with special notice**.
8. Quoting thresholds under the wrong labour law (10 vs 20 employees).
9. In ethics answers, listing the seven principles without **explaining** each in one line.
10. Writing long paragraphs – use numbered points and headings.